

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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UNITED STATES OF AMERICA :

- v. - :

INDICTMENT

ROBERT COPLAN, :

(S1) 07 Cr. 453 (SHS)

MARTIN NISSENBAUM, :

RICHARD SHAPIRO, :

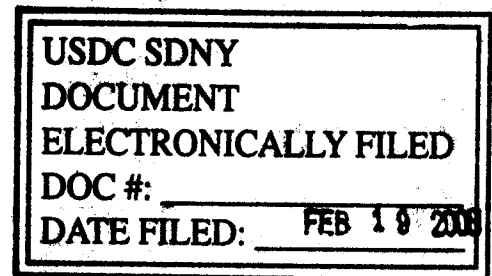
BRIAN VAUGHN, :

DAVID L. SMITH, and :

CHARLES BOLTON, :

Defendants. :

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COUNT ONE

(Conspiracy)

The Grand Jury charges:

Background

1. At all times relevant to this Indictment, Ernst & Young ("E&Y") was one of the largest accounting firms in the world. E&Y provided audit services to many of the world's largest corporate clients, and provided tax services to corporate and individual clients, including some of the wealthiest individuals in the United States. Those tax services included preparing tax returns, providing tax advice and tax planning advice, and representing clients in audits by the Internal Revenue Service ("IRS") and litigation with the IRS in Tax Court.

2. At all times relevant to this Indictment, as part of its tax practice, E&Y had a business unit that was responsible for providing tax advice, as well as financial planning advice, to individuals. That business unit was known as Personal Financial Counseling, or

“PFC.” E&Y had partners and other professionals throughout the country who were members of the PFC practice.

3. At all times relevant to this Indictment, E&Y also had a department within its tax practice known as the National Tax Department (“National Tax”). The individuals assigned to National Tax were generally experts in particular areas of taxation, and they provided expert tax advice to E&Y professionals in the field. Within National Tax was a sub-group of experts whose particular areas of expertise related to E&Y’s PFC practice.

4. In or about early 1998, the national leader of PFC formed a group that would devote itself to designing, marketing, and implementing high-fee tax strategies for individual clients. These strategies included tax shelters that could be used by high-net-worth clients to eliminate, reduce or defer taxes on significant income or gains. The group initially called itself the “VIPER Group” (an acronym for “Value Ideas Produce Extraordinary Results”), but changed its name to the “Strategic Individual Solutions Group,” or “SISG,” in or about early 2000.

5. Defendants ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO and BRIAN VAUGHN (“the E&Y defendants”) were members of the VIPER/SISG group for all or a significant part of the period relevant to this Indictment. The E&Y defendants worked together with banks, financial institutions, investment advisory firms, law firms and others, including defendants DAVID L. SMITH and CHARLES BOLTON, to design, market and implement tax shelters called CDS (“Contingent Deferred Swap”); COBRA (“Currency Options Bring Reward Alternatives”); CDS Add-On; and PICO (“Personal Investment Corporation”).

6. The tax shelters developed by the VIPER/SISG group were marketed to clients and prospective clients by members of the group, as well as by PFC professionals located throughout the country, who had primary responsibility for client contact. In or about mid-1999, certain PFC professionals around the country were designated to be members of the “Quickstrike Team,” a nationwide area-based network created to provide greater efficiency in the marketing and execution of the VIPER/SISG strategies, including tax shelters.

The Defendants

7. At all times relevant to this Indictment, defendant ROBERT COPLAN, a lawyer with a Master’s Degree in tax law, was a partner located in E&Y’s Washington, D.C. office. COPLAN worked within the PFC section of National Tax, and was one of E&Y’s “subject matter experts,” or “SMEs,” in the areas of personal income taxes, estate and gift taxes, and excise taxes. COPLAN, who was the National Director of E&Y’s Center For Family Wealth Planning, was a member of the VIPER/SISG group from its inception in or about early 1998. For most of the next several years, COPLAN supervised the activities of the group. Among his other activities, COPLAN approved promotional materials, and ensured that essential information about the design and implementation of E&Y’s tax shelters was shared throughout the PFC practice. He consulted regularly with defendants MARTIN NISSENBAUM, RICHARD SHAPIRO and BRIAN VAUGHN, and also participated in sales presentations to clients. Before his employment at E&Y, COPLAN had worked for the IRS as a Branch Chief in the Legislation and Regulations Division.

8. At all times relevant to this Indictment, defendant MARTIN NISSENBAUM, a lawyer with a Master's Degree in tax law, was a partner at E&Y. Located in E&Y's New York office, NISSENBAUM was a member of the PFC group within National Tax, and was a subject matter expert in the areas of individual income taxation, retirement benefits and compensation. NISSENBAUM was the National Director of E&Y's Personal Income Tax and Retirement Planning practice, and was a member of the VIPER/SISG group from its inception. Among other things, NISSENBAUM worked closely with defendants ROBERT COPLAN and RICHARD SHAPIRO in evaluating and developing the various tax shelters marketed by the group, and participated in sales presentations to clients and prospective clients.

9. At all times relevant to this Indictment, defendant RICHARD SHAPIRO, a lawyer with a Master's Degree in tax law, was a partner located in E&Y's New York office. SHAPIRO was a subject matter expert in the taxation and structuring of financial products and instruments. Although he was not a formal member of National Tax or the VIPER/SISG group until 2000, SHAPIRO worked regularly with the group from its inception in or about early 1998. SHAPIRO worked closely with defendants ROBERT COPLAN and MARTIN NISSENBAUM in evaluating the shelters marketed by the group. Because of his background and expertise in financial instruments, he played an essential role in the approval process of several of the group's shelters. He also participated in sales presentations to clients and prospective clients. Before his employment at E&Y, SHAPIRO had been the Director of Tax for the Financial Services Industry Practice at another large accounting firm.

10. At all times relevant to this Indictment, defendant BRIAN VAUGHN – who had a college degree in accounting – was a certified public accountant (CPA) and a certified

financial planner (CFP). After working at three other major accounting firms, VAUGHN joined E&Y as a senior manager in 1998. As a member of the VIPER/SISG group from its inception through at least 2001, VAUGHN led sales efforts for most of the SISG shelters, and also played a development role. VAUGHN was promoted to partner in or about 2002, in large part based upon his role in successfully developing and marketing E&Y's tax shelters.

11. Defendant DAVID L. SMITH was a lawyer with a master's degree in business administration (MBA) and a CPA. During the period from approximately 1978 through 1996, he worked at several major accounting firms and brokerage houses, where he helped design and develop various tax strategies and tax shelters. In 1997, SMITH joined an investment advisory firm, where he developed, marketed and implemented tax shelters, including CDS. SMITH left that firm in 1998, and soon afterward co-founded the Private Capital Management Group ("PCMGM"). PCMGM marketed and implemented tax shelters, including CDS. While at PCMGM, SMITH – who was the 50% owner of the company – marketed and implemented CDS with the E&Y defendants, as well as with defendant CHARLES BOLTON. SMITH also assisted the E&Y defendants and BOLTON in marketing the CDS Add-On shelter in 2000. During the period from 1999 through 2000, SMITH earned millions of dollars from his involvement in CDS.

12. From in or about 1999 through at least in or about 2006, defendant CHARLES BOLTON owned and operated a group of companies ("the Bolton companies") that implemented and assisted in implementing tax shelters for E&Y's clients. BOLTON – who studied business finance in college – held a series of finance jobs during the period from 1983 through 1992. In 1992, BOLTON formed the first of his own companies, Bolton Financial

Services. In or about mid-1999, BOLTON met defendant DAVID L. SMITH, and soon afterward began to assist SMITH in implementing CDS for E&Y's clients. In or about early 2000, BOLTON arranged for one of his companies to license the CDS idea from SMITH. BOLTON thereafter assisted in further developing and implementing CDS, together with E&Y. In or about mid-2000, BOLTON agreed to assist the E&Y defendants in marketing and implementing the CDS Add-On shelter. During the period from 1999 through 2002, BOLTON made millions of dollars from his involvement in CDS and CDS Add-On.

Tax Shelter Fraud

13. During the period from in or about 1998 through in or about 2006, the defendants, ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, DAVID L. SMITH and CHARLES BOLTON, and others known and unknown to the Grand Jury (hereinafter "the co-conspirators"), participated in a scheme to defraud the IRS by designing, marketing, implementing and defending tax shelters using means and methods intended to deceive the IRS about the bona fides of those shelters, and about the circumstances under which the shelters were marketed and implemented.

14. The defendants and their co-conspirators designed, marketed, implemented and defended these tax shelters so that wealthy individuals with taxable income generally in excess of \$10 or \$20 million could eliminate or reduce the individual income taxes they would have to pay to the IRS. As designed, marketed and implemented, instead of wealthy clients paying U.S. individual income taxes that were legally owed (generally, between 20% and 40% of their taxable income), the clients could pay total costs calculated largely as a percentage of the desired tax loss or deduction generated by the particular tax shelter. These costs included

the fees payable to E&Y and the other participants, including PCMG, the Bolton companies, the various law firms that supplied opinion letters to the clients, and the banks and other financial institutions that executed the transactions. The costs also included an amount that would be used to execute purported "investments," which were designed, in part, to disguise and conceal the true nature and purpose of the tax shelters.

15. The defendants and their co-conspirators understood that if the IRS were to detect the clients' use of these tax shelters, and learn the true facts and circumstances surrounding the design, marketing and implementation of these shelters, the IRS would aggressively challenge the claimed tax benefits. In that event, the IRS would seek to collect the unpaid taxes plus interest, and might also seek to impose substantial penalties upon the clients. Accordingly, the defendants and their co-conspirators undertook to prevent the IRS from: a) detecting their clients' use of these shelters; b) understanding how the steps of the transactions operated to produce the tax results reported by the clients; c) learning that these shelters were marketed as cookie-cutter products that would eliminate, reduce or defer large tax liabilities; d) learning that the clients had not undertaken these transactions because they were seeking profit-making investment opportunities, but had instead done so because they were seeking huge tax benefits; and e) learning that, from the outset, all the clients intended to complete a pre-planned series of steps that had been designed by the conspirators to lead to the specific tax benefits sought by the clients.

16. In order to maximize the appearance that the tax shelters were investments undertaken to generate profits, and to minimize the likelihood that the IRS would learn the transactions were actually designed to create tax losses and deductions, the defendants

and their co-conspirators created, assisted in creating, and reviewed transactional documents and other materials containing false and fraudulent descriptions of the clients' motivations for entering into the transactions, and for taking the various steps that would yield the tax benefits. They also carefully protected internal documents and promotional materials that set forth the tax benefits and pricing schedules of the various shelters against disclosure to the IRS. The conspirators' goal of deceiving the IRS into believing that the tax shelters were driven by investment objectives rather than tax savings objectives was demonstrated in an email sent by defendant ROBERT COPLAN to a PFC professional in 2001. That individual had prepared a proposed client solicitation letter, in which he provided short descriptions of various SISG strategies and their accompanying tax benefits. COPLAN expressed reservations about sending such a letter to clients, as the IRS would inevitably ask the clients for marketing and promotional materials in the course of any audit. COPLAN explained, "Since our ultimate goal is to make our strategies appear to be investment techniques that have advantageous tax consequences, letters like this are not helpful to the client's case[.]"

17. The law in effect at all times relevant to this Indictment provided that if a taxpayer claimed a tax benefit by using a tax shelter, and that benefit was later disallowed, the IRS could impose substantial penalties upon the taxpayer -- ranging from 20% to 40% of the underpayment attributable to the shelter -- unless the claimed tax benefit was supported by an independent opinion, reasonably relied upon by the taxpayer in good faith, that the tax benefit "more likely than not" would survive IRS challenge. In order to encourage clients to participate in the shelters, and to shield the clients from possible penalties, the defendants worked with law firms that agreed to provide E&Y's clients with opinion letters that claimed the tax shelter losses

or deductions would “more likely than not” survive IRS challenge, or “should” survive IRS challenge. However, the defendants knew those opinions were based upon false and fraudulent statements, and omitted material facts. By helping their clients obtain false and fraudulent opinion letters, with the understanding and intent that those opinion letters would be presented to the IRS if and when the clients were audited, the defendants not only sought to undermine the ability of the IRS to ascertain the clients’ tax liabilities, but also sought to undermine the ability of the IRS to determine whether penalties should be imposed.

18. The defendants and their co-conspirators undertook these actions so that E&Y, PCMG, the Bolton companies and the other entities involved could participate in the highly lucrative tax shelter market in which other accounting firms and “investment advisory” firms were already participating; so that E&Y could prevent its high-net-worth clients from taking their business (including, potentially, the highly-prized audit business associated with some of these individuals) to its competitors; so that PFC – a business unit that was not a substantial contributor to the firm’s revenues – could grow and prosper within the firm; so the individual E&Y defendants could enhance their own opportunities for professional recognition, advancement, job security, and remuneration; and so the Bolton companies could obtain access to E&Y’s high net worth clientele for purposes of developing future business.

19. In addition to implementing fraudulent tax shelters for E&Y’s clients, in 2000, defendants ROBERT COPLAN, MARTIN NISSENBAUM and RICHARD SHAPIRO implemented a tax shelter to evade their own taxes, and arranged for eight of their E&Y partners to participate in the transaction with them. Use of that tax shelter enabled the group of eleven E&Y partners to eliminate a total of approximately \$3.7 million in taxes.

20. In addition to implementing fraudulent tax shelters for E&Y's clients, in 2000 and 2001 defendant CHARLES BOLTON implemented fraudulent tax shelters to reduce and defer his own tax liabilities. Use of those tax shelters enabled BOLTON to reduce his tax liabilities by millions of dollars.

The Fraudulent CDS Shelters

21. CDS (an abbreviation for "Contingent Deferred Swap") was marketed and sold by E&Y from mid-1999 through 2001. During that period, approximately 69 CDS transactions were implemented for approximately 140 of E&Y's wealthy clients. As designed and marketed, E&Y's fee for CDS was approximately 1.25% of the tax deductions to be generated for each client. Various clients paid greater or lesser amounts, but ultimately the transaction generated more than \$27 million in fees for E&Y. Clients who implemented CDS also paid fees to other participants in the transaction, including at least 1.25% to PCMG (for CDS transactions implemented in 1999) or the Bolton companies (for CDS transactions implemented in 2000 and 2001), as well as a fee to Law Firm A for an opinion stating that if the IRS were to disallow the CDS tax benefits, the client "should" ultimately prevail (a "should opinion"). Typically, Law Firm A's fee was at least \$50,000.

22. The objective of CDS was to convert a client's ordinary income into long-term capital gains, and defer the client's tax liability from the year in which the income was earned ("Year 1") to the following year ("Year 2"). During the period when CDS was sold, ordinary income for very wealthy individuals was typically taxed at a rate of approximately 40%, while long-term capital gains were taxed at approximately 20%. Accordingly, the conversion of

a client's income from the ordinary rate to the capital gains rate resulted in tax savings to the client of approximately 20% of their income. CDS was marketed to individuals or groups of individuals who had at least \$20 million in ordinary income to shelter.

23. Although there were variations, in a typical CDS transaction, the client sought to convert \$20 million in ordinary income into capital gains. CDS was designed and implemented as a series of pre-determined steps intended to deceive the IRS by making it appear that the client was engaged in the business of currency trading for profit, and that the various component parts of the transaction were routine financial activities comprising a coherent business philosophy. The conspirators concealed the fact that CDS was mass-marketed to clients who had no genuine interest in putting their money at risk by engaging in the business of currency trading, but were instead merely carrying out steps they were told to carry out in order to achieve CDS's tax benefits. These steps, and the manner in which these steps were manipulated to deceive the IRS, included the following:

a) The CDS strategy was implemented through the creation of a limited partnership in which an entity characterized as an investment advisor was the general partner and E&Y's client was the limited partner. Defendant DAVID L. SMITH's company, PCMG, was the general partner for the CDS partnerships set up in 1999. After CHARLES BOLTON licensed CDS from SMITH in early 2000, one of the Bolton companies -- Bolton Capital Planning ("BCP") -- became the general partner for the CDS partnerships set up in 2000 and 2001. Although the main purpose for creation of each CDS limited partnership was for the client to obtain tax benefits, and for E&Y, PCMG, and the Bolton companies to earn tax shelter fees, the documents created to execute the transaction described each partnership as a "trading

partnership,” and made no mention of the tax benefits, but instead stated that the partnership was “organized to generate capital appreciation.”

b) After determining how much ordinary income the client wished to shelter from taxes in Year 1, the conspirators would typically arrange for the client to contribute approximately one-third of that amount (\$6.6 million in the typical example) to the purported “trading partnership.”

c) The success of the client’s tax position with the IRS required that the partnership be characterized for tax purposes as a “trade or business,” so that “business deductions” could be generated, and then used by the clients to offset their taxable income. Accordingly, the conspirators arranged for approximately \$1 million of the client’s \$6.6 million contribution to be placed in a trading account. In order to make it appear that the “trading partnership” was genuinely engaged in the “business of trading for profit,” the funds in that trading account were generally used to carry out a high volume of short-term trades. However, the activity in that account consisted largely of trades designed to preserve the client’s capital, so the funds in the account could be returned to the client once the tax benefits of CDS had been obtained. As described by a co-conspirator employed by one of the Bolton companies in an email to another co-conspirator, “Our true investment objective in the various trading accounts was minimal gains and losses.” As stated by the same co-conspirator in an email sent to defendant CHARLES BOLTON and others, “I am happy to report that ... [f]or the most part we were down an average of approximately 1% on all of the trading accounts. In my eyes, that is 100% in line with what our objective was.” The conspirators affirmatively sought to conceal the fact that no trading profits were expected, as reflected in an email sent by another co-conspirator

in February 2000, asking that certain references be removed from CDS documents, and explaining, “We don’t want to highlight that we don’t anticipate trading profits.”

d) A portion of the client’s cash contribution to the “trading partnership” (approximately \$5 million in the example) was put toward a \$20 million swap contract, which was entered into between the partnership and a bank or financial institution (“the bank”). The swap contract called for the “trading partnership” to make periodic payments totaling approximately \$20 million to the bank over the life of the swap. Because the payments made to the bank in Year 1 were made by an entity purportedly engaged in the “business” of trading, those payments were claimed by the partnership as “business deductions.” The purported “business deductions” – which flowed through the “trading partnership” to the client – would be used to offset the \$20 million in ordinary income earned by the client in Year 1, and thus would eliminate the client’s tax liability that year.

e) In order for a CDS client to shelter \$20 million in income, it was necessary, under the tax code, for that client to have \$20 million “at risk” in the CDS transaction. In a typical transaction, only \$5 million of the client’s contribution was put toward the swap; the additional \$15 million was obtained by the partnership as a purported “loan” from the bank. However, the so-called “loan” from the bank did not involve any actual disbursement of funds to the CDS partnership. Instead, the bank merely made a “book entry” indicating that loan proceeds were being deposited into a collateral account at the bank. The CDS swaps were structured so that no real funds were transferred to the control of the partnership, and there was no possibility that any real funds of the bank would be placed at any risk of loss. Because the bank was at all times fully collateralized on the “loan,” there was also no possibility of a default on the “loan” by

the partnership. The conspirators caused the CDS clients to execute documents by which they agreed to accept personal liability on the loans, while at the same time assuring the clients that they would not have to contribute any additional money to the transaction. In causing the clients to execute such documents, the conspirators sought to deceive the IRS into believing that the individual clients were actually “at risk” for the loan amounts. In truth and in fact, they knew that no such risk existed, that the so-called “loans” served no business purpose, and that the “loans” served only to increase the amount of the tax deduction the individual could claim. This tax purpose is reflected in a 1998 email concerning the CDS transaction, sent between employees of the bank that executed the 1999 CDS transactions for E&Y’s clients:

You are right to say that the collateral is part funded out of our loan and, to that extent, seems non-sensical, but there is a tax reason why this circularity is necessary. . . . (You will recall that the purpose of the trade is to convert current income into long-term capital gains.) . . . Incidentally, this “loan” has zero capital implications for the bank.

f) The CDS swap contract also provided for a “termination payment” to be paid by the bank to the CDS partnership in Year 2, at the end of the swap. For a \$20 million swap, the termination payment was approximately \$20 million, with some variation based on market fluctuation. In order for the termination payment made to the CDS partnership to qualify for long-term capital gains treatment, the swap termination in Year 2 had to occur more than a year after the swap was executed, and had to be characterized as an “early termination” of the swap contract. Although prospective CDS clients were told by E&Y that the swaps would last for just over one year, the conspirators arranged for swap contracts to be drawn up with 18-month maturity dates. This was done to mislead the IRS into believing that the

parties actually contemplated an 18-month swap, and that “early termination” was an option, but not a foregone conclusion. The conspirators sought to conceal this plan from the IRS, as reflected in an email sent by defendant BRIAN VAUGHN to a co-conspirator in June 2001. In that email, VAUGHN suggested removing reference to “early termination” from a CDS economic model, explaining, “This could adversely affect our tax situation given the level of audits that are currently in progress. . . . Remember our goal is to convince the agents the client did not have a predisposition of early termination.” For a similar reason, defendant RICHARD SHAPIRO recommended against use of an internal E&Y document called a “CDS Action Plan,” which set forth all the steps of the transaction in advance, including early termination of the swap. In an email SHAPIRO sent to defendants ROBERT COPLAN, MARTIN NISSENBAUM and BRIAN VAUGHN, he explained:

[O]ne of the problems with tax advantaged transactions when they are viewed is that they are perceived (correctly I might add) as too scripted. While having a plan is important, should we have in writing ‘before the fact’ such things as the fact that our swap will be terminated early? Clearly, that is necessary for the flow of the transaction. But should there be a document in existence (such as this) that has all the chapters and verses laid out? I question that seriously.

Thus, by manipulating the terms of the swap and by concealing the genuine intentions of all the parties, the conspirators concocted a scenario that enabled them fraudulently to characterize the termination payments received by the CDS partnerships from the bank as long-term capital gains. Those capital gains flowed through the partnerships to the clients, so the clients could be taxed at the lower, capital gains rate.

24. As part of the scheme to defraud the IRS, the conspirators created additional documents that purported to provide non-tax business motivations for steps that were actually tax-motivated. For example, defendant ROBERT COPLAN drafted a letter to be signed by clients who had decided to terminate their CDS partnerships after the tax benefits had been obtained. In that letter, the clients falsely attributed their decision to discontinue their trading activities to the September 11, 2001 terrorist attacks, and to “possible economic repercussions resulting from such attacks.” In an email sent to various members of E&Y’s PFC practice, as well as to defendants MARTIN NISSENBAUM and RICHARD SHAPIRO, COPLAN attached his draft letter, and explained that the letter could be used “as a means of establishing a logical reason for winding down the trading account in the partnership. . . . This could document for the file a logical non-tax rationale for ending the trading account – if that is otherwise what the client wants to do.” A copy of COPLAN’s email and the attached letter was forwarded to defendant CHARLES BOLTON.

25. As part of executing the fraudulent CDS tax shelters, the conspirators arranged for CDS clients to sign false factual representations that could be, and were, incorporated into the CDS opinion letters prepared by Law Firm A. For example, although the real purpose of the CDS trading activity was to achieve a particular volume and frequency of trading so the conspirators could plausibly characterize the CDS partnerships as involved in a “trade or business,” and could thereby assert that the swap payments made by the partnerships in Year 1 were “business deductions,” the CDS clients were directed to sign, and did sign, a document stating, “I regard the various investments of the partnership -- including the swaps and the trading activities -- as comprising one coherent business philosophy, and this diversity of

investments was an important element in my decision to invest in the partnership.” In truth, as the conspirators well knew, the diversity of investments was not an important element in the clients’ decisions, and the only “coherent philosophy” reflected in the various components of the CDS transaction was a philosophy to reduce taxes.

26. In addition to incorporating the false factual representations described in paragraph 25, above, the defendants and their co-conspirators caused Law Firm A to issue opinion letters which they knew contained false and fraudulent statements and omitted material facts, including but not limited to the following:

a) The opinions stated that the objective of the partnership’s trading activities was to “profit from short term market movements,” when in reality, the primary objective of the trading activity was to achieve a particular volume and frequency of trades, while preserving the client’s capital by minimizing trading losses.

b) The opinions stated that because either party to the swap contract could elect to terminate the swap early, the partnership was “not in control of that decision, should it occur,” and therefore the partnership should not be viewed as “being able to manipulate the timing of income,” when in reality, both parties to the swap contracts planned to terminate the swaps early from the outset, and the sole purpose of that plan was to manipulate the timing of income.

c) The opinions stated that the limited partner (the client) was “at risk” for an amount greater than the amount invested because the client had agreed to be personally liable for the debts of the partnership, when in reality, the clients had been assured that they would not be liable for any amount over their initial cash contribution, and the transaction

was arranged so there would be no such liability.

d) The opinions stated that “[n]one of the business conducted by the Partnership [had] a predetermined outcome,” when in reality, the E&Y defendants and their co-conspirators had marketed to E&Y’s clients, and the clients had paid fees to obtain, a strategy consisting of a pre-planned series of steps leading to a predetermined tax benefit.

e) The opinions did not disclose that the client’s primary purpose for implementing the CDS transaction was to obtain the tax benefits, or that the fees associated with the transaction were calculated on the basis of the intended tax deduction to be generated.

f) The opinions did not disclose that they were rendered by an attorney who had assisted the defendants in designing, marketing, and implementing the CDS transaction, and had been offered to the clients as part of a promotional package.

The Fraudulent COBRA Shelters

27. COBRA (an acronym for “Currency Options Bring Reward Alternatives”) was marketed and sold by E&Y during the last few months of 1999 to 51 wealthy taxpayers. Of the 16 COBRA transactions, all but one were implemented in late 1999; the other was implemented in 2000. Although some clients paid greater or lesser amounts, as designed and marketed, E&Y’s fee was approximately 1.5% of the tax losses to be generated using the strategy, and COBRA generated approximately \$14.7 million in fees for E&Y. The fees paid by COBRA clients amounted to approximately 4.5% of the losses to be generated, including a fee of just under 3% charged by the law firm of Jenkins & Gilchrist (“J&G”). J&G prepared most of

the transaction documents for the COBRA shelters, and implemented the COBRA transactions for the clients. J&G also issued “more likely than not” opinion letters to the COBRA clients. Defendants ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO and BRIAN VAUGHN realized that because J&G was involved in designing, structuring and implementing the transaction, the clients would not be able to obtain penalty protection on the basis of J&G’s opinion letter. Therefore, the E&Y defendants arranged for another attorney, a partner at Law Firm B, to issue each of the COBRA clients a second “more likely than not” opinion for a fee of up to \$150,000.

28. The objective of COBRA was the complete and permanent elimination of all tax liability on whatever amount of ordinary income or capital gain a client might choose. COBRA, which involved the manipulation of basis in digital foreign currency options, was E&Y’s brand of a strategy also known as the “digital option trade” or the “short option strategy.”

29. COBRA was designed, marketed and implemented as a series of pre-planned steps which, within a period of 30 to 45 days, would generate artificial losses sufficient to offset a client’s income or gains completely. COBRA was intended to deceive the IRS by making it appear that the client – together with other like-minded individuals – was “investing” in foreign currency options in order to make a profit, and that non-tax business reasons existed for the various steps of the transaction. In reality, in exchange for substantial fees that were calculated largely as a percentage of the tax loss to be generated for E&Y’s clients, the E&Y defendants and their co-conspirators provided the clients with a cookie-cutter transaction that utilized pairs of almost completely offsetting foreign currency options to generate huge artificial tax losses. Although the options had some chance of earning the clients a profit after the fees

were paid, this so-called “investment” opportunity was not offered generally through E&Y’s Investment Advisory Service, but was instead marketed to a select group of individual clients with more than \$20 million in income or gains to offset.

30. COBRA included the following key steps:

a) The client would identify an amount of ordinary income or capital gains on which the client wished to eliminate taxes. The client or E&Y would then identify other individuals who also wished to eliminate their taxes, with whom the client could participate in the transaction.

b) Using J&G, each client would create a wholly-owned limited liability company (“LLC”). That LLC would purchase a digital foreign currency option (the “long option”) from a bank, and would sell an almost completely off-setting digital foreign currency option (“the short option”) to the same bank. The client’s LLC paid a net amount to the bank for the pair of options; that amount equaled 5% of the tax loss the client wished to generate (in other words, 5% of the income the client wished to offset).

c) The pair of offsetting options constituted a single financial bet between the client and the bank that, at the end of 30 days, a particular currency would have gone up or down in value against another currency by a specific amount. The option pairs were priced and structured by arrangement between E&Y and the bank so that if the client won the bet (or, was “in the money”) at the end of the 30-day period, the bank would pay the client an amount sufficient to yield a profit over and above the client’s initial 5% contribution plus the fees associated with the transaction. E&Y told its clients that the odds of that happening were approximately 38%. If the client lost the bet (or, was “out of the money”) after 30 days, then the

client would lose his 5% contribution and his fees. E&Y told its clients that the likelihood of that outcome was approximately 62%. Thus, the E&Y defendants and the clients knew from the outset that the clients would probably lose their 5% contribution and their fees.

d) Almost immediately after acquiring the option pair or pairs from the bank, each client – acting through his newly created LLC – would contribute the option pairs to a newly created partnership, also formed by J&G, in which one or more other COBRA clients were also partners. After approximately 30 days, the options would expire. Each client would also contribute a low-value asset to the partnership – an ordinary asset or a capital asset, depending on whether the client desired ordinary or capital losses.

e) Each client would then transfer his partnership interest to a new S-Corporation, also formed by J&G. When this occurred, the partnership would automatically terminate. According to the E&Y defendants and their co-conspirators, each client could then claim – for tax purposes – that his tax basis in the partnership was equal to the cost of the long option (which had been calculated intentionally to equal the income the client wished to offset), rather than the net amount actually paid by the client to participate in the transaction (5% of the price of the long option). The conspirators claimed that the low-value asset contributed by the client to the partnership would take on that high tax basis when the partnership terminated, so that when the S-Corporation sold the low-value asset at fair market value only days later, a huge artificial loss – equal to almost twenty times the client's initial cash contribution – was created for the client.

31. The E&Y defendants and their co-conspirators were aware that if the IRS were to discover all the facts surrounding the design, marketing and implementation of COBRA,

and that the COBRA clients were primarily or exclusively motivated by a desire to eliminate huge tax liabilities, the IRS would aggressively challenge the claimed tax benefits. Accordingly, among other steps they took to prevent the IRS from learning those facts, the conspirators: 1) falsely and misleadingly represented the COBRA clients' motivations for entering into the transaction, and for taking the various steps necessary to create the huge artificial losses; 2) encouraged COBRA clients to engage in activities designed to disguise and conceal their tax motivations for entering into the transaction; 3) falsely represented to the IRS the likelihood that clients could earn a profit from COBRA; 4) directed the destruction of documents which would reveal the true facts surrounding the design, marketing and implementation of COBRA; 5) caused and approved the issuance of false and fraudulent opinion letters; and 6) misled the IRS during audits of the COBRA transaction.

32. Among the ways in which the conspirators sought to conceal the fact that COBRA was tax-motivated, and was designed and implemented as a pre-planned series of steps, were the following:

- a) Defendant ROBERT COPLAN directed that client engagement letters make no reference to tax losses, or to the fact that fees were calculated as a percentage of the tax losses the clients sought to generate.
- b) Defendant ROBERT COPLAN directed that PowerPoint presentations which laid out all the steps of the COBRA transaction not be left with clients.
- c) In addition to having clients contribute 5% of the desired loss amount to the transaction, the E&Y defendants directed clients to contribute an additional 2% of the desired loss amount to the COBRA partnerships, and recommended using that additional cash

to engage in trading activity. The sole purpose of that trading activity was to deceive the IRS into believing that the COBRA partnerships had been formed to conduct investment activities, and not merely to generate tax losses. The E&Y defendants' intent to deceive the IRS in this regard was reflected in a series of emails sent by defendant ROBERT COPLAN to various PFC members whose clients had initiated COBRA transactions, as well as to defendants RICHARD SHAPIRO, MARTIN NISSENBAUM and BRIAN VAUGHN. COPLAN explained in the first email, "[T]he more trading activity the better [because] the trading activity is important to the maintenance of a business purpose for the partnership." In a later email he advised, "Trades should occur weekly in the partnership, with weekly turnover of positions at or near 100% The tax position will be aided if there is at least some type of trading activity[.]"

d) Defendant ROBERT COPLAN sent an email to PFC professionals, with a copy to defendants RICHARD SHAPIRO, MARTIN NISSENBAUM and BRIAN VAUGHN, suggesting that their COBRA clients download foreign currency trading information from a website, and explaining that such material could be useful "as file material to evidence investigation into currency trading."

e) After the COBRA partnerships terminated in late 1999, and after the artificial losses had been generated, the E&Y defendants recommended that clients maintain the 2% cash contribution in their S-Corporations, and continue to engage in trading activities. This step was designed to deceive the IRS into believing that the S-Corporations had been created for some actual business purpose, instead of simply to achieve COBRA's tax benefits. In an email to PFC professionals in January 2000, defendant ROBERT COPLAN stated that he, together with defendants MARTIN NISSENBAUM and RICHARD SHAPIRO, were "providing

guidance . . . as to what is recommended to strengthen the client's tax position[.]” COPLAN continued:

It is preferable to leave the S Corp in place through the end of the year 2000 to enhance the substance of the transaction – i.e., so that the entire structure is not closed down within two months. . . . As for activity in the account we believe ‘The more the better’ [because] the tax position will be strengthened by significant trading activity

With respect to the S-Corporation, COPLAN explained to another PFC member, “The longer it runs, the better it looks from a business standpoint as to why the thing was formed.”

f) After the IRS began auditing COBRA clients, defendant ROBERT COPLAN sent an email to PFC professionals throughout the country, directing that they destroy COBRA documents. The email was titled “Important - Purge Of All Key COBRA Documents,” and it instructed that recipients “immediately delete and dispose of” COBRA documents such as PowerPoint slides and work plans.

33. As part of the COBRA client's fees, the client received two “more-likely-than-not” opinion letters, one from J&G, and the second from Law Firm B. The E&Y defendants and their co-conspirators knew that these opinion letters contained false and fraudulent statements, and omitted material facts.

a) J&G's opinions were false and fraudulent for the following reasons, among others: i) they stated that the clients had made factual representations to J&G concerning their reasons for entering into the transaction, when in reality, no such factual representations had been made to J&G; ii) they stated that the clients had contributed their foreign currency options to the COBRA partnerships for “substantial non-tax business reasons,”

when in reality, there were no substantial non-tax business reasons for that step, and the clients took that step because the conspirators directed them to do so; and iii) they stated that the clients had contributed their partnership interests to the S Corporations for “substantial non-tax business reasons,” when in reality, there were no substantial non-tax business reasons for that step, and the clients took that step because the conspirators directed them to do so.

b) Law Firm B’s opinions were false and fraudulent for the following reasons, among others: i) they stated that the clients had contributed their foreign currency options to the COBRA partnerships for “substantial non-tax business reasons,” when in reality, there were no “substantial non-tax business reasons” for that step, and the clients took that step because the conspirators directed them to do so; ii) they stated that the clients had contributed their partnership interests to the S Corporations for “substantial non-tax business reasons,” when in reality, there were no “substantial non-tax business reasons” for that step, and the clients took that step because the conspirators directed them to do so; and iii) they stated that “there existed no understanding, obligation or agreement” under which the clients committed to undertake the various steps in the COBRA transaction, when in reality, the COBRA clients had been told they could obtain the promised tax benefits only if all the steps were completed, and therefore the clients intended to complete them.

c) The J&G opinions purported to be based upon “all the facts and circumstances necessary” for J&G to form its opinion, and Law Firm B’s opinions purported to be based upon all “pertinent facts.” However, the J&G opinions failed to disclose that J&G had implemented the COBRA transaction on behalf of the clients, and that J&G had collected as its fee a percentage of the loss amount generated. In addition, neither opinion disclosed the

following material facts, among others: i) that most of the COBRA clients responded to a promotional pitch that emphasized COBRA's tax benefits, and they entered into the transaction primarily or exclusively to obtain those tax benefits; ii) that the clients knew from the outset that a particular series of steps would be undertaken, for a given fee, leading ultimately to a specific tax result; iii) that COBRA was structured so that each client would probably lose his entire cash contribution plus fees, rather than make any profit; and iv) that the "more likely than not" opinion letters had been offered to the clients as part of E&Y's promotion of the shelter.

34. On or about January 5, 2000, E&Y's management decided that E&Y would no longer market COBRA to its clients. That decision was reached after subject matter experts outside the VIPER/SISG group expressed the view that COBRA would not survive scrutiny under applicable law. Among the objections raised by others within E&Y was that COBRA did not have a meaningful "business purpose."

The Fraudulent CDS Add-On Shelters

35. CDS Add-On, which involved adding a COBRA-like transaction onto a CDS transaction, was marketed for a brief period in mid-2000. Approximately 61 wealthy individuals took part in a total of 37 Add-On transactions, which generated more than \$24 million in fees for E&Y. CDS Add-On was implemented by defendant CHARLES BOLTON through the Bolton companies, and generated millions of dollars in fees for BOLTON and the Bolton companies. In addition to the fees paid to E&Y, the Bolton companies, and other participants in the transactions, clients paid \$75,000 for a "more likely than not" opinion letter from Law Firm A.

36. The objective of CDS Add-On was for the client to defer indefinitely the income tax liability on the capital gains generated in the second year of the CDS transaction. In most cases, CDS Add-On consisted of two parts: 1) a two-year CDS transaction that would result in capital gains to the CDS partnership; and 2) a COBRA-like strategy that would generate artificial losses for the CDS partnership, and thus offset those capital gains. However, unlike in COBRA, the losses generated using CDS Add-On did not permanently eliminate taxes, but instead resulted in a tax deferral for as long as the income to be sheltered remained in the hands of the partnership.

37. The second part of the transaction (the COBRA-like structure, referred to as the “Add-On”) was implemented by having each participating CDS partnership acquire one or more pairs of almost completely off-setting digital foreign currency options. As in COBRA, the premium for the long options equaled the amount of income the client wished to offset. Thus, each client’s partnership could acquire options that would offset the capital gains received in the second year of CDS, or the partnership could acquire options with a higher premium, and thereby shelter additional income or gains. Participating partnerships would then contribute their option pairs to a new entity, BCP Trading & Investments, LLC (“BCPT&I”), which was created by defendant CHARLES BOLTON and was used solely to implement the Add-On shelter. By contributing their option pairs to BCPT&I, the CDS partnerships became members of BCPT&I. Before the end of the tax year in which the client wanted to shelter their CDS capital gains (Year 2 of the CDS transaction), the CDS partnership would withdraw from BCPT&I, and would receive foreign currency which – as in COBRA – took on an artificially inflated tax basis. The CDS partnership would then sell or exchange the foreign currency to trigger a loss equal to the

capital gain from the CDS swap termination payment, or such larger amount as the client had chosen. The client's taxes would be deferred until cash was removed from the CDS partnership, or until that partnership terminated.

38. Like CDS, the Add-On transaction also involved a so-called "loan" from a financial institution. Just as the "loan" made to the partnership in CDS involved no genuine transfer of funds and served no purpose other than to generate tax benefits, the "loan" extended to the Add-On clients was also made with a "book entry" and served no purpose other than to assist the clients in claiming artificial tax losses.

39. The idea for CDS Add-On arose in or about early May 2000, after a similar idea was described to defendant BRIAN VAUGHN. VAUGHN passed the idea to defendant ROBERT COPLAN in an Instant Message ("IM"), stating, "If we could integrate CDS and the foreign currency trading program with the short option transaction, we could have a great transaction." COPLAN responded that he would consider VAUGHN's proposal, and forwarded the IM to defendants MARTIN NISSENBAUM and RICHARD SHAPIRO.

40. During the next several weeks, the E&Y defendants developed the Add-On strategy, and obtained the participation of defendant CHARLES BOLTON. The E&Y defendants were well aware that only a few months earlier, E&Y's management had decided that COBRA would no longer be marketed by E&Y, and that others within E&Y would oppose the Add-On strategy unless it had a more meaningful business purpose than COBRA. In order to provide the Add-On strategy with such a "business purpose," and thus to obtain approval to market Add-On, the E&Y defendants created a false cover story: they claimed that the idea for the CDS partnerships to purchase the digital foreign currency options, and the idea to consolidate

those options in a new LLC, had come from one of the traders who was managing activity in the CDS partnership trading accounts on behalf of BCP, and that the purpose of those steps was “to diversify trading and enhance performance” in the trading accounts. They also falsely claimed that the plan to take those steps had been presented to them by defendant CHARLES BOLTON, and that they had merely recognized the favorable tax consequences that could be obtained.

According to defendant ROBERT COPLAN, these events were simply a “fortuitous circumstance.”

41. In reality, there was no way the Add-On transaction could “enhance performance” in the CDS trading accounts. Unlike the COBRA transaction, which entailed a foreign currency bet that could actually result in a profit for the client if the client’s option pair ended up “in the money,” no such possibility existed for the Add-On transaction. This was because the Add-On client was required to contribute only about 0.5% of the desired loss amount to the Add-On transaction (as opposed to 5% contributed by the COBRA client). Although the payout on a successful Add-On bet was 2:1, any profit potential on such a payout was far exceeded by the amount the client was required to pay in fees to E&Y, the Bolton companies, Law Firm A and the financial institution involved. Thus, the Add-On transaction carried no reasonable possibility of profit; it served no purpose other than to defer the client’s tax liability indefinitely, and to generate fees for the other participants.

42. The conspirators agreed, with respect to the marketing of Add-On, that PCMG (the general partner of the CDS partnerships set up in 1999) and BCP (the general partner of the CDS partnerships set up in early 2000) would send letters to the CDS clients, announcing the opportunity to participate in a new “program” that would diversify their trading returns and

enhance performance. Defendant DAVID L. SMITH signed the letters sent on behalf of PCMG, and Belle Six – a co-conspirator not named as a defendant herein, who served as a Managing Director of BCP – signed the letters sent on behalf of BCP. Defendant ROBERT COPLAN also drafted a letter to be sent to the CDS clients by E&Y. In that letter – which was sent to defendants MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN and CHARLES BOLTON to review and edit – COPLAN also referred to BCP’s desire “to diversify trading and enhance performance.” As COPLAN explained in an email to the E&Y defendants, he deliberately drafted the letter in such a way as to conceal the fact that withdrawal from the BCPT&I – a step necessary to generate the artificial losses that would defer the client’s taxes – was planned from the outset: “I softened the last reference to the liquidation of the interest in the LLC so it sounds less like an event that we know will happen in the near future.” These letters were prepared in anticipation of possible future audits, in order to deceive the IRS into believing that the transaction was motivated by investment concerns, and that the steps leading to the tax result were not pre-planned from the outset.

43. In order for the many steps of the Add-On shelter to be implemented efficiently for all the CDS clients who wished to participate, defendant DAVID L. SMITH agreed to transfer from PCMG to BCP the control of all 1999 CDS partnerships whose limited partners wished to participate in Add-On. This was accomplished through three agreements executed in July 2000, all of which were signed by both SMITH and defendant CHARLES BOLTON. BCP thereafter served as the general partner for all the CDS partnerships that implemented Add-On shelters, and ensured that all the necessary steps were executed on behalf of each one.

44. During the marketing of CDS Add-On in 2000, the E&Y defendants took additional steps to ensure that the true motivation behind the strategy was not revealed. A PowerPoint presentation was created by an individual outside the VIPER/SISG group, to illustrate the inter-relationship between CDS and CDS Add-On, and it was distributed to PFC personnel. In a series of emails that followed, defendant ROBERT COPLAN expressed concern that the PowerPoint presentation would undermine the story the conspirators had constructed to establish a business purpose for the strategy, and would thus reveal the tax motivation behind it:

a) On June 14, 2000, COPLAN sent an email to defendants BRIAN VAUGHN and RICHARD SHAPIRO, explaining that the Add-On strategy would “lose all of its business purpose if it is reduced to steps in a PowerPoint slide. The tax objective will appear to be the driving force rather than the money manager’s interest in consolidating the accounts.”

b) The same day, COPLAN sent an email to all the PFC personnel who had received the PowerPoint presentation, stating that the slides were for internal use only, and were not to be shown when presenting CDS to clients. COPLAN cautioned, “There should be no materials in the client’s hands – or even in their memory – that describe CDS as a single strategy that includes the Add-on feature.”

c) COPLAN then wrote to the individual who had prepared the PowerPoint slides:

I hope you can understand the problem with portraying the strategy as an integrated transaction designed to produce a capital gain deferral. If these slides ever made their way to the IRS . . . the entire business purpose argument that gives us the ability to distinguish this from COBRA would be out the window. Since we

got the internal OK to do this add-on feature on the basis that there is a much stronger business purpose than we had with COBRA, doing anything to undermine that business purpose would be creating unnecessary risk for our clients and unnecessary risk for the PFC practice.

45. In an email to defendant ROBERT COPLAN, defendant RICHARD SHAPIRO also expressed his concern about linking the two strategies, stating, "I remain concerned of the formal pre-wired tie-in to cobra. I think it adversely impacts the story that we can tell regarding the purpose of the transaction."

46. In addition to offering the Add-On shelter to partnerships that had been created in order to participate in CDS, the E&Y defendants offered Add-On to several existing entities that were genuinely engaged in the business of trading options, but which had not participated in the CDS tax shelter. Representatives of these entities met with E&Y personnel, and were offered the opportunity to reduce and defer the owners' income tax liabilities by acquiring pairs of digital currency options, which would ultimately be contributed to BCPT&I, together with the digital option pairs acquired by the CDS partnerships. Several such entities agreed to participate.

47. In July and August 2000, after pairs of digital options were acquired for the various Add-On participants, defendant CHARLES BOLTON signed documents directing that all the digital option pairs be transferred from accounts held by the CDS partnerships to an account held by BCPT&I. BOLTON also caused the digital option pairs purchased by the entities described in paragraph 46, above, to be transferred from accounts held by those entities to the account held by BCPT&I.

48. After the digital option pairs had all been transferred to BCPT&I, additional steps were taken to further deceive the IRS about the reason the clients entered into the Add-On transaction. For example, in November 2000, the conspirators crafted a letter for Add-On clients to submit to BCP, expressing either interest or disinterest in participating in a “second round of digital option purchases.” In reality, there was no plan for BCP to engage in a “second round of digital option purchases,” and this letter was designed purely to create the false impression that the decision of the particular Add-On clients to withdraw from BCPT&I or to remain as members – a decision that would determine whether each client’s artificial tax loss would be triggered in 2000 or 2001 – was made for business reasons rather than tax reasons. The real purpose of the “second round of digital option purchases” letter is illustrated in emails sent by defendant ROBERT COPLAN to PFC personnel whose clients had implemented Add-On transactions, as well as to defendants MARTIN NISSENBAUM, RICHARD SHAPIRO and BRIAN VAUGHN. In an email dated November 8, 2000. COPLAN explained:

Belle Six has sent you a letter (sample below) intended for each of your CDS Add-On clients. The letter mentions that the Bolton LLC into which the . . . trading account was transferred is considering doing a second round of digital option trading. The client is offered the option of declining to participate in this digital activity, in which case he is to notify Bolton (Belle Six) by written reply, thereby triggering the termination of their partnership’s interest in the LLC. . . . Those of you advising clients whose CDS partnerships will remain active into 2001 to maintain deferral should be aware that the letter does not mean that [Bolton] will **actually** be investing in new digitals – only that they are **considering it**.

One recipient of COPLAN’s email who was apparently unsure how to advise his client responded:

Our client ... is a CDS 2000 client (with add on) – we do not want to redeem the LLC interest and trigger the loss until 2001 (when the capital gain from the CDS 2000 will result). Therefore, I assume that our client should not sign the letter (even though they are not necessarily interested in doing more digitals for investment purposes). Correct?

COPLAN replied, “You are correct. The only clients who should sign the letter are those who want to be redeemed out of the LLC this year. The fact that your client does not sign the letter does not mean that more digitals will in fact be acquired.”

49. Steps were also taken to conceal from the IRS the fact that the “loans” purportedly extended in connection with the Add-On transaction were not real loans but were instead “book entries” made so that the Add-On clients would have sufficient basis in their CDS partnerships to deduct their Add-On tax losses. After the financial institution that had supposedly funded the “loans” provided a sample statement reflecting interest payments to and from the partnerships, Belle Six, a co-conspirator not named as a defendant herein, commented on the format of the statement in an email defendant CHARLES BOLTON and others within the Bolton companies:

I like that we have statements that show the date of the loan . . . ;
I like that we can see both interest earned/paid. The thing that concerns me is that on one statement we are showing that we took out a loan that is 100% fully collateralized. In other words, we have made it easy to ask the question, “What is the purpose of the loan?” I have copied BV to ask his opinion.

Defendant BRIAN VAUGHN responded to Belle Six in an email she forwarded to BOLTON and the others. VAUGHN stated:

I agree with your comments. The clients should love this format. It is very easy to follow. However, I don't think [the Law Firm A lawyer] would want to see this schedule nor the IRS. It clearly demonstrates the loan is used to obtain tax basis and not for investment. . . . Maybe if we could demonstrate the client is staying in "cash" for a short period of time . . . it would disguise the tax basis loan issue.

50. In addition, with knowledge that the financial institution that extended the so-called "loans" would not actually allow real funds to be used by the partnerships, defendant CHARLES BOLTON sent a letter to the financial institution that was designed to conceal that fact. By pre-arrangement with the financial institution, BOLTON's letter said:

It is the intention of BCP to utilize the proceeds of these loans to invest in securities and trading strategies other than [financial institution's] paper. As such, we would like to inquire on [your] willingness to remove some of the restrictions that are currently in place with regards to the proceeds of the loan. It is the intent of BCP to handle each partnership on a case by case basis. Please let us know your decision on our request as soon as possible as it is our desire to move forward with these trading strategies promptly.

A representative of the financial institution then assisted in concealing that the loans were not genuine by responding:

I am in receipt of your letter dated February 16, 2001. Let me assure you that [financial institution] will be flexible as possible with transactions of the various CDS partnerships. We will review each request on a case by case basis. Please consider me as your point person for your requests and I will review each one personally.

51. As part of executing the fraudulent Add-On tax shelter, the conspirators arranged for Add-On clients to sign representation letters prepared by Law Firm A, which contained false and misleading factual representations that could be, and were,

incorporated into Law Firm A's Add-On opinion letters. For example, each client signed a document stating, among other things, that the client regarded the various activities of the partnership – specifically including the client's "investment" in BCPT&I – as comprising "one coherent business philosophy." In truth, as the conspirators well knew, the acquisition of the digital option pairs and the contribution of those option pairs to BCPT&I was not an "investment" at all, and was not part of any "coherent business philosophy."

52. As part of executing the fraudulent CDS Add-On tax shelter, defendant CHARLES BOLTON also signed representation letters prepared by Law Firm A, which contained false and misleading factual representations that could be, and were, incorporated into Law Firm A's opinion letters. For example, with knowledge that no genuine "loan proceeds" were available for use by the partnerships that participated in Add-On, BOLTON signed documents which stated:

I intend to utilize Loan funds, as appropriate, to leverage the existing trading programs of the Partnership and/or invest in other programs, designed to yield returns in excess of the cost of funds while minimizing risk to capital, such as strategic investments in sovereign debt with manageable currency risk.

53. In order to persuade the IRS that the tax results achieved through the Add-On strategy were allowable, and to avoid the imposition of penalties on clients if the IRS were to disallow those results, the defendants and their co-conspirators caused Law Firm A to issue opinion letters which they knew contained false and fraudulent statements and omitted material facts, including but not limited to the following:

a) The opinions stated that “organization of the LLC was based upon probability analysis and engaging a well reputed expert in the largest and most active trading market in the world . . . in order to profit from a trading program,” when in reality, BCPT&I was organized at the behest of the E&Y defendants, who recognized that the purported “trading program” carried no chance of generating a profit, but would generate tax benefits for the clients and fees for the conspirators.

b) The opinions stated that “[n]one of the business conducted by the Partnership or the LLC [had] a predetermined outcome” and that “[n]one of the transactions . . . [were] prearranged or structured to yield a predetermined economic result,” when in reality, E&Y had marketed to its clients – and the clients had paid fees to obtain – a strategy consisting of a pre-planned series of steps leading to a predetermined tax benefit.

c) The opinions stated that the partnership’s “decision to maintain an investment in the LLC or terminate such investment [was] no different than any other investment decision exhibited by the Partnership,” when in reality, the partnership’s decision to terminate its membership in BCPT&I was not an investment decision at all, but was based solely on the timing of desired tax losses.

d) The opinions stated that the business purpose of BCPT&I was “asset appreciation,” when in reality, the digital option pairs contributed to BCPT&I were likely to expire “out of the money,” and they carried no practical possibility of a profit for the clients even if they expired “in the money.”

e) The opinions stated that the loan funds obtained in connection with the transaction would be used “to opportunistically invest in trading or other programs,” and

accordingly, that the loan would likely be treated as a “genuine indebtedness.”

f) The opinions failed to disclose that the purpose for entering into the Add-On transaction was for participating E&Y clients to obtain tax benefits, and that the fees associated with the transaction were calculated on the basis of the intended tax losses to be generated.

g) The opinions failed to disclose that they were rendered by an attorney who had assisted the defendants in designing and implementing the transaction, and therefore were not independent.

The Fraudulent PICO Shelters

54. PICO was marketed and sold during 2000 and 2001. E&Y implemented approximately 96 PICO transactions for approximately 150 wealthy individuals. E&Y generated more than \$56 million in fees from PICO, charging its clients approximately 2% of the tax losses the clients sought to generate. Each PICO client was provided with a “more likely than not” opinion letter from one of two law firms, Law Firm C and Law Firm D; the fees for those letters ranged between \$50,000 and \$100,000, depending on the size of the transaction.

55. The objective of PICO was to defer taxation and, in some cases, to convert ordinary income into capital gains, thus reducing the client’s tax rate. Within a period of a few months, a PICO client would follow a pre-planned series of steps, and generate artificial losses that could be used to defer taxes indefinitely on the income the client wanted to shelter.

56. PICO included the following essential steps:

a) A client seeking to defer tax liability would form an S-Corporation (a “Personal Investment Corporation,” or “PICO”), together with one or two individuals affiliated with an entity which described itself as an “investment advisor,” and which purported to have special trading expertise (“Company Z”). The client was a 20% shareholder in the PICO, and the other individuals were 80% shareholders (“the Company Z shareholders” or the “majority shareholders”). The PICO client funded the S-Corporation with an amount equal to approximately 4% of the tax loss the client wanted to generate (in other words, 4% of the income the client wished to shelter from taxes).

b) Company Z would then use those funds to engage in trading activity, entering into financial instruments commonly known as “straddles.” The “straddles” were designed to generate essentially off-setting gains and losses, which could be realized for tax purposes, or “triggered,” separately. By pre-arrangement, the trading would be carried out for approximately 60-90 days, and then the gains would be triggered. When that occurred, 80% of the gains would be allocated to the majority shareholders for tax purposes, and only 20% of the gains would be allocated to the client.

c) By further pre-arrangement, the client would then buy out or “redeem” the Company Z shareholders from the PICO. At that point, the client would be the 100% shareholder. Once the client was the 100% shareholder, the losses would be triggered, and 100% of the losses (an amount roughly equivalent to the amount of income the client was seeking to shelter) would be allocated to the client for tax purposes. These losses were artificial losses, in that there were no corresponding economic losses suffered by the client.

d) In order for the client to claim the full benefit of the losses generated, the client would then contribute additional assets to the PICO entity. As long as the additional assets remained in the PICO entity, the tax liability on the client's income would be deferred. When the assets were removed from the entity, those assets would be taxed at the capital gains rate.

57. As the conspirators knew, in order for the PICO strategy to survive IRS scrutiny, it required a non-tax "business purpose." With knowledge that the true motivation behind the strategy was for the clients to obtain tax benefits, the conspirators developed a false cover story to explain to the IRS – if the client were audited – why the client created an S-Corporation together with the Company Z shareholders, only to "buy out" those shareholders after 60-90 days. According to the cover story, each client formed an S-Corporation because the client wanted to use that entity as their principal investment vehicle, and because the client wanted to achieve asset protection and estate planning objectives. The client included the Company Z shareholders in the S-Corporation, according to the cover story, in order to "try out" Company Z's trading strategy, and the client intended to make a decision at the end of 60 or 90 days -- based on trading performance -- whether to continue with that strategy. According to the story, if the client was satisfied with the trading strategy, the client would buy out the other shareholders, and then enter into a two-year asset management agreement with Company Z, or with one of Company Z's affiliates, so that the client could continue to enjoy the benefit of Company Z's special trading expertise.

58. In addition to developing the false cover story, the conspirators took other steps to conceal from the IRS the fact that PICO was primarily, if not exclusively, tax-motivated,

and that it was designed, marketed and implemented as a pre-planned series of steps. Among other things:

a) The E&Y defendants developed and used promotional materials that referred to PICO as “a long-term personal investment vehicle, integrating investment management services with estate planning and asset protection services.”

b) Defendant ROBERT COPLAN directed that no promotional materials be left with clients, in order to prevent those materials from falling into the hands of the IRS. In an email sent in June 2001 to PFC personnel, as well as to defendants MARTIN NISSENBAUM, RICHARD SHAPIRO and BRIAN VAUGHN, COPLAN stated, “PICO slides are not to be left with clients, and this is a policy we must all adhere to. This is ultimately for the client’s protection.” In a later email, also sent to PFC personnel and to his co-defendants, COPLAN remarked that “a fax of the materials to certain people in the . . . government would have calamitous results,” and he urged, “Please take us seriously when we instruct that you not leave PICO materials behind at your presentations. . . . Impress upon [prospective PICO clients] that it [is] for their protection should they proceed with the strategy that we are not leaving them behind (i.e., in the event of an audit).”

c) Defendant ROBERT COPLAN opposed a proposal by one PFC professional to provide clients with a work plan that laid out the steps of the transaction. In an email copied to defendant RICHARD SHAPIRO, COPLAN stated, “[A]fter we go to the trouble to make sure the client does not have any documents that walk through the steps of the transaction, I cannot imagine that we would want to hand him a work plan that shows each minute step including the redemption of the S shareholder. I would strongly advise against

providing a written document to the client that lays out these steps as a prearranged plan.”

d) Defendant ROBERT COPLAN directed that a promotional brochure developed by Company Z, and biographical information concerning Company Z’s officers, be provided not only to prospective PICO clients, but also to clients who had already completed PICO transactions. He explained that these documents “convey necessary information for the client to have made an informed decision to embark on a new investment program with [Company Z].”

e) Although E&Y’s fee for the PICO transaction was calculated as approximately 2% of the loss the client wished to generate, defendant ROBERT COPLAN directed that a fee of only \$50,000 be listed in the client’s engagement letter.

f) The conspirators arranged for the balance of E&Y’s fee to be paid by the client to Company Z or to one of its affiliates, and for Company Z’s affiliate then to pay the remainder to E&Y. In order to justify such large payments from Company Z’s affiliate to E&Y, the conspirators created a phony contract under which E&Y claimed to have performed consulting services to the affiliate. Those contracts – which were actually created and signed well after most of the clients’ PICO fees had already been passed through the affiliate to E&Y – were back-dated in order to make this discrepancy less obvious. Defendant RICHARD SHAPIRO’s concern that the so-called “consulting contract” for the 2000 PICO transactions had not been executed as of April 2001 was reflected in an email he sent to individuals at Company Z and Law Firm C, in which he stated, “I STILL DO NOT HAVE THE TAX CONSULTING AGREEMENT FROM LAST YEAR. WITH MOST OF THE PAYMENTS MADE UNDER THAT AGREEMENT ALREADY, DON’T YOU THINK WE (AND YOUR CLIENTS)

SHOULD HAVE A FINAL DRAFT THAT CAN BE SIGNED?????? WE MUST HAVE SOMETHING FOR OUR FILES.”

g) After it became apparent that PICO clients were not inclined to continue conducting trading activities in their PICO entities after redeeming the Company Z shareholders, the E&Y defendants encouraged them to do so in order to protect the clients’ claims that the PICO transaction was not tax-motivated. In a March 2001 email to PFC personnel, with copies to his three E&Y co-defendants, defendant ROBERT COPLAN explained, “When the PICO strategy was developed, E&Y and [Company Z] understood that the client’s representations regarding his non-tax investment motives and expectation of a pre-tax profit would depend on maintaining trading activity after the 80% shareholders were redeemed.” COPLAN observed that this was apparently “not the preferred approach of clients,” and therefore, that PFC personnel had to “establish some guidelines and properly manage client expectations[.]” The problem continued; a few months later, COPLAN followed up with a similar email, reiterating the need for clients to engage in trading activity in their PICO entities, and stating, “Because we see reports that this is not the direction certain clients are headed in, we feel it necessary to establish some guidelines.”

59. In order to persuade the IRS that the tax results achieved through the PICO strategy were allowable, and to avoid the imposition of penalties on clients if the IRS were to disallow those results, the conspirators arranged for Law Firm C and Law Firm D to provide the clients with opinion letters. The E&Y defendants and their co-conspirators knew these opinion letters contained false and fraudulent statements and omitted material facts, including but not limited to the following:

a) The opinion letters stated that the PICO S-Corporations were not formed to avoid or evade federal income taxes, but were instead designed to facilitate investment activities, provide asset protection and achieve estate planning objectives. In reality, as the conspirators well knew, the S-Corporations were formed precisely so that clients could avoid or evade taxes.

b) The opinion letters stated that the Company Z shareholders became investors in the various PICOs in order to demonstrate the potential return available through interest rate arbitrage trading activity, when in reality, this step was necessary to accomplish the desired tax results.

c) The opinion letters stated that the trading strategy was not designed to produce a predetermined result, when in reality, E&Y had marketed to its clients, and the clients had paid fees to E&Y and Company Z to obtain, a strategy consisting of a pre-planned series of steps leading to a predetermined tax benefit.

d) The opinions issued by Law Firm C failed to disclose that they were rendered by an attorney who had assisted the E&Y defendants and the principals of Company Z in designing, marketing, and implementing the transaction, and therefore were not independent.

The IRS's 2002 Voluntary Disclosure Initiative

60. In or about December 2001, the IRS announced a program under which taxpayers who had engaged in tax shelters could voluntarily disclose those transactions to the IRS, in exchange for amnesty from penalties that might otherwise be imposed if the IRS were to

audit the transactions and find a tax underpayment. In order to qualify for the program, taxpayers were required to disclose the transaction to the IRS, and to include in their disclosures, among other things, a statement describing the “material facts” of the transaction; the names and addresses of parties who had promoted, solicited or recommended the transaction to the taxpayer, and parties who had collected fees from the transaction; a statement agreeing to provide various documents and materials relating to the transaction, including marketing materials and legal opinions; and a statement signed by the taxpayers, under penalties of perjury, that the taxpayers had examined their disclosures, and that to the best of their knowledge and belief, the disclosures contained all the relevant facts and were true, correct and complete.

61. During 2002, defendants ROBERT COPLAN, MARTIN NISSENBAUM and RICHARD SHAPIRO prepared, and assisted in preparing, templates that could be used by E&Y clients who had engaged in tax shelters, and who wished to participate in the IRS’s voluntary disclosure initiative in order to eliminate the possibility of IRS penalties. Although COPLAN, NISSENBAUM and SHAPIRO knew that participation in the program required the submission of a “true, correct and complete” disclosure to the IRS of “all relevant facts” in a statement that would subject their clients to penalties of perjury, they drafted template disclosure letters that contained many of the same false and fraudulent statements that had previously been included in transaction documents and opinion letters, and omitted many of the same material facts. Tax shelter clients who participated in the voluntary disclosure initiative thereafter submitted false, fraudulent and incomplete statements to the IRS.

The E&Y Promoter Penalty Audit

62. In or about April 2002, the IRS began an examination of whether E&Y had complied with various legal requirements applicable to the firm's tax shelter activities. In connection with that examination – commonly referred to as a “promoter penalty audit” – the IRS sought documents and sworn testimony from individuals knowledgeable about the VIPER/SISG tax shelters. In June and August of 2002, defendants ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO and BRIAN VAUGHN appeared before the IRS to answer questions. After being placed under oath, they sought to obstruct and impede the IRS by providing false and misleading testimony concerning the origin, design, marketing and implementation of E&Y's tax shelters.

a) Among other things, COPLAN provided the following false and misleading testimony: that E&Y had no involvement in the operation of the CDS trading partnerships; that the CDS clients were not sure whether the CDS swaps would terminate early, and thus did not know whether the income they received in the second year of the swap would be characterized as capital gains; that the fees charged to CDS clients were “fixed fees” rather than fees calculated based on a percentage of the tax benefits; that when E&Y became involved with CDS Add-On, the CDS partnerships were already planning to consolidate digital options in a single LLC, and that E&Y learned about the plan as a “fortuitous circumstance”; that no promotional materials had been distributed or shown to CDS Add-On clients because COPLAN and others “didn't think the transaction was that complicated”; that the fees paid by the PICO investment advisor to E&Y were paid “for consulting with them on the tax aspects of the PICO transaction”; and that the reason an S-Corporation was used for PICO instead of a partnership

was that clients viewed the S-Corporation as a “good family investment vehicle.”

b) Among other things, VAUGHN provided the following false and misleading testimony: that the VIPER/SISG group was not involved in the wide-spread marketing of tax shelters, but instead merely responded to questions and proposals that came from clients; that the CDS Add-On transaction was brought to E&Y’s attention by defendant CHARLES BOLTON, who had already created a fund, and had offered E&Y’s clients an opportunity to participate in that fund; that the digital options used in the Add-On transaction were purchased “from the investment standpoint,” and were “just part of [the client’s] investing”; that the fees charged by E&Y for the digital option transactions were “fixed fees” calculated based on E&Y’s assessment of how much time would be spent by particular E&Y personnel involved with a particular transaction for a specific client; that E&Y did not set fees based upon a percentage of tax results; that E&Y “typically” encouraged its clients to use their own counsel, and recommended counsel if the clients felt their own counsel were “not competent in digital option taxation”; that the VIPER/SISG group maintained no database of documents relating to its tax shelters; that E&Y did not develop its own brand of digital option trade, and that there was “no tax strategy, per se, that was developed internally by E&Y’s individual tax practice”; that there were no predetermined tax benefits for the Add-On strategy, and that “it was very difficult” to estimate the Add-On tax benefits until after the transactions were complete; and that he could not recall the nature of COPLAN’s involvement in the Add-On strategy, or that SHAPIRO provided the subject matter expertise for the digital option transactions.

c) Among other things, NISSENBAUM provided the following misleading testimony: that the CDS partnership was a “trading partnership”; and that the

partnership “would be trading in short-term securities to get as much short-term profit as possible.”

d) Among other things, SHAPIRO provided the following false and misleading testimony: that E&Y “received fees for tax consulting services” provided to Company Z in connection with the development of PICO; and that COBRA was designed to provide an investor with the ability to obtain a return of approximately 31% with “a probability of success of just under 40%.”

The BCP Promoter Penalty Audit

63. In or about May 2004, the IRS began an examination of whether BCP had complied with various legal requirements applicable to the firm’s tax shelter activities. In connection with that promoter penalty audit, the IRS sought documents and information from BCP. In responding to those requests for information and documents, representatives of BCP produced to the IRS various false and fraudulent documents, including opinion letters issued by Law Firm A for the CDS and Add-On, representations letters relating to the opinions issued for CDS and Add-On, and loan agreements, notes and guarantees relating to Add-On.

IRS Examinations of the Various Tax Shelters

64. As a result of information provided in connection with the voluntary disclosure initiative, as well as information produced by E&Y and the Bolton companies during the promoter penalty audits, and in taxpayer audits, the IRS undertook detailed examinations of many of the CDS, COBRA, CDS Add-On, and PICO shelters. In connection with these examinations, the IRS sent Information Document Requests (“IDRs”) to many of

E&Y's individual tax shelter clients, and to many of the entities created by the conspirators in order to execute the tax shelters. Those IDRs sought additional information, and requested production of various documents. Defendants ROBERT COPLAN, MARTIN NISSENBAUM and RICHARD SHAPIRO, together with others at E&Y, participated in the production of information and documents to the IRS in response to those IDRs. Defendant CHARLES BOLTON, together with others at the Bolton companies, also participated in the production of information and documents to the IRS in response to those IDRs. In that process, many of the false and fraudulent explanations and cover stories that had been created by the conspirators to conceal the tax motivations behind the shelters were presented to the IRS, and many of the false and fraudulent documents that had been created by the conspirators to conceal those tax motivations – including opinion letters and correspondence – were produced to the IRS. The IRS also took sworn testimony from various individuals involved in the marketing and implementation of the shelters, including clients, financial advisors to clients, E&Y personnel, and defendants DAVID L. SMITH and CHARLES BOLTON.

65. Represented by attorneys and professionals provided by E&Y, various tax shelter clients and their financial advisors gave false and misleading testimony and statements to the IRS concerning, among other things, the clients' motivations for entering into the tax shelter transactions in question.

66. On or about December 9, 2003, defendant DAVID L. SMITH gave sworn testimony to the IRS concerning one of the CDS transactions implemented in 1999 by PCMG. Among other things, SMITH falsely testified that he not explained the tax ramifications of CDS to the bank that implemented the transaction, and that he had not received any money from

defendant CHARLES BOLTON in connection with CDS. In reality, SMITH had explained the tax ramifications to the bank, and BOLTON had paid SMITH \$3.75 million to license CDS.

67. On or about April 12 and 13, 2005, defendant CHARLES BOLTON gave sworn testimony to the IRS concerning two CDS transactions implemented by BCP in 2000. Among other things, BOLTON falsely testified that E&Y never indicated that the CDS swaps would terminate early; that the decision to terminate the swaps was based on “economics”; that there was no understanding or agreement – either written or non-written – that the swaps would terminate early; and that he did not recall what tax benefits CDS clients could receive based on their loans.

**The E&Y Partners’ Own Fraudulent Tax Shelter
(The “Tradehill” Transaction)**

68. In addition to designing, marketing and implementing fraudulent tax shelters for clients and prospective clients of E&Y, defendants ROBERT COPLAN, MARTIN NISSENBAUM and RICHARD SHAPIRO developed and utilized a tax shelter to evade their own taxes, and assisted eight other E&Y partners to do the same. The strategy they employed was a short option strategy, similar to a COBRA shelter.

69. In or about late 1999 or early 2000, E&Y announced a proposal to sell its global consulting business to a French company called Cap Gemini. In that transaction, E&Y partners would receive shares of stock in the new company. Those shares would be denominated in euros, and would not be transferable for a period of time that was unknown, but that was expected to exceed four years. Although the stock received by the partners could not be sold, the E&Y partners were told that their receipt of the stock would constitute income on which they

would be taxed in 2000. Accordingly, in order to assist the partners in paying their tax liabilities on the stock received, E&Y proposed to sell some of the Cap Gemini stock at the time of the transaction, and to give each partner – in addition to shares of Cap Gemini stock – cash that could be used by that partner to cover his or her 2000 personal income tax liability generated by receipt of the stock.

70. After a vote of E&Y's partners, the transaction took place in or about May 2000, and on or about May 23, 2000, defendants ROBERT COPLAN, MARTIN NISSENBAUM, and RICHARD SHAPIRO, as well as other E&Y partners, each received a distribution of Cap Gemini stock. An amount of cash was set aside by E&Y for their use in paying income taxes on the stock they received.

71. Upon learning of the intended Cap Gemini transaction, defendant MARTIN NISSENBAUM began discussing with other E&Y partners the possibility of using a tax shelter to eliminate the income tax liability arising from their receipt of the Cap Gemini stock. By late October 2000, a group of eleven E&Y partners, including defendants ROBERT COPLAN, MARTIN NISSENBAUM, and RICHARD SHAPIRO, had decided to form an entity called Tradehill Investments, LLC ("Tradehill"), and to use Tradehill to carry out a transaction similar to COBRA, thereby eliminating all or most of their tax liability on the Cap Gemini stock ("the Tradehill transaction"). The three defendants undertook to act as representatives for the other E&Y partners.

72. In order to execute the transaction, defendant MARTIN NISSENBAUM, working in conjunction with a tax shelter promoter and with attorneys from Law Firm D, created Tradehill, in which all eleven E&Y partners were members. The Operating Agreement for

Tradehill falsely stated that Tradehill was organized “for investment purposes.” The defendants created a second entity called Churchwind Investments, LLC (“Churchwind”), which was wholly owned by Tradehill. The Operating Agreement for Churchwind – which was signed by NISSENBAUM, as well as by defendants ROBERT COPLAN and RICHARD SHAPIRO – falsely stated that Churchwind was organized “for investment purposes.”

73. The eleven members of Tradehill collectively contributed \$350,000 in cash, and on or about November 1, 2000, defendant MARTIN NISSENBAUM caused Churchwind to acquire three almost completely offsetting pairs of euro/dollar currency options. The premiums paid for the three long options totaled \$25 million, but the actual cost to the partners (the “net premium”) was only \$350,000. The three option pairs all had different maturity dates, one in April 2001, one in May 2001, and one in June 2001.

74. On or about November 13, 2000, defendant MARTIN NISSENBAUM, acting on behalf of the group, caused Tradehill to contribute the three pairs of currency options to an entity called AD International FX Fund, LLC (“ADFX”), in exchange for 90% ownership of ADFX. The other two owners of ADFX were tax shelter promoters who had contributed a total of \$30,000 in cash to the entity.

75. In or about mid-December 2000, ADFX closed out one of the euro/dollar option pairs that had been contributed by Tradehill, and purchased shares of stock. Then, on or about December 19, 2000, defendant MARTIN NISSENBAUM caused Tradehill to resign from ADFX in exchange for stock, dollars and euros worth approximately \$187,246. At that time, none of the three option pairs contributed to ADFX by Tradehill was “in the money,” and the maturity dates of the three options were approximately four, five and six months away.

76. On or about December 26, 2000, defendant MARTIN NISSENBAUM caused Tradehill to distribute the stock it had received upon resignation from ADFX to two new entities, Hiddenbrook Holding, LLC (“Hiddenbrook”), and Greenoak Holdings, LLC (“Greenoak”). Hiddenbrook – which had been created only days earlier – had five members, including defendants MARTIN NISSENBAUM, ROBERT COPLAN and RICHARD SHAPIRO. The members of Greenoak – which had also been created only days before – were the other six E&Y partners. The same day, NISSENBAUM directed the immediate sale of the stock distributed to Hiddenbrook, and a member of Greenoak directed that Greenoak’s shares be sold. The shares were sold the following day, triggering artificial losses.

77. From in or about December 2000 through in or about mid-April 2001, an attorney at Law Firm D, working together with defendant MARTIN NISSENBAUM, drafted a legal opinion. The opinion was intended to be used to support the position that the losses triggered by the sale of stock by Hiddenbrook and Greenoak could be used by the eleven E&Y partners to eliminate the tax liability related to their Cap Gemini stock, and to protect the eleven partners against IRS penalties.

78. In connection with the drafting of that opinion, defendant MARTIN NISSENBAUM assisted in preparing a “Certificate of Facts.” The “Certificate of Facts” – which contained false and fraudulent statements – was intended to be incorporated by reference into Law Firm D’s opinion, and was intended to deceive the IRS into believing that the E&Y partners executed the various steps of the Tradehill transaction for investment reasons rather than tax reasons. Among other things, the document falsely stated: 1) that “[t]he purpose and purchase and sale of [the] Options [was] that Tradehill believed that such investments could result in

substantial profits with only limited downside risk”; 2) that Tradehill contributed its membership interest in Churchwind to ADFX to “diversify its risk”; 3) that Tradehill’s “primary motivation” in participating in the transaction “was to attain, on a risk-adjusted basis, an attractive return on its investment . . . without regard to tax benefits”; and 4) that “the decision to withdraw from [ADFX] was based on a variety of factors, including anticipated future market conditions, currency exchange rates, interest rates, the availability of alternative investments, and Tradehill’s financial situation.”

79. In or about April 2001, Law Firm D – which had assisted the defendants in creating the entities used to execute the shelter – issued a back-dated opinion letter to Hiddenbrook and Greenoak. The opinion letter incorporated the false statements contained in the “Certificate of Facts” described in paragraph 78, above. In addition, the opinion letter falsely stated, among other things, that all “pertinent facts” relating to the transaction had been set forth in the opinion.

80. From in or about April 2001 through in or about October 2001, defendants ROBERT COPLAN, MARTIN NISSENBAUM and RICHARD SHAPIRO, as well as their eight partners, filed tax returns on which they used the losses generated through the Tradehill transaction to eliminate tax liability on all or most of the income they received in the form of stock and cash from the Cap Gemini transaction.

81. In or about May 2003, the IRS notified the eleven participants in the Tradehill transaction that their 2000 tax returns were being audited. In connection with that audit, the IRS sent each of the eleven partners who had participated in the Tradehill transaction an Information Document Request (“IDR #1”), requesting both information and documents. The

members of the group made arrangements for an attorney at Law Firm D to represent them in responding. Defendant MARTIN NISSENBAUM assisted that attorney in drafting responses on behalf of each partner to IDR #1, as well as to a second IDR ("IDR #2") and a third IDR ("IDR #3"). Copies of the partners' letters to the IRS were sent to defendant MARTIN NISSENBAUM.

82. The responses to IDR #2 were sent to the IRS on or about September 25, 2003. Those responses contained false and misleading statements, including but not limited to the following: 1) statements that the E&Y partners had entered into the Tradehill transaction in order to generate profits, when in reality the transaction had no reasonable possibility of generating a profit; 2) a statement that the Tradehill transaction was intended fully to hedge the partners' exposure to fluctuation in the euro, when in reality, the transaction had no capacity to do so; 3) a statement that there were no unwritten understandings between the participants in the Tradehill transaction, when in reality, there was an understanding among all the parties to the transaction that the E&Y partners would exit their option positions before the end of 2000, in order to claim tax losses they could use to offset their Cap Gemini income; and 4) a statement that there was no expectation or referral of any future business to Law Firm D, when in reality, in 2001, the defendants referred PICO clients to Law Firm D for opinion letters.

Charles Bolton's Own Fraudulent Tax Shelters

83. In 2000 and 2001, in addition to implementing fraudulent tax shelters for clients of E&Y, defendant CHARLES BOLTON utilized CDS tax shelters to reduce and defer his own tax liability on income he earned from implementing CDS and CDS Add-On for numerous clients. In order to carry out the first CDS transaction, BOLTON caused the creation

of BIG Trading Partners, L.P. (“BIG Trading Partners”) in October 2000. BCP was the general partner of BIG Trading Partners, and BOLTON was the limited partner.

84. In or about October 2000, defendant CHARLES BOLTON caused BIG Trading Partners to enter into two swaps with a financial institution. As structured, those swaps were designed to generate a business deduction for BOLTON of approximately \$15 million in 2000. As part of the 2000 CDS transaction, BOLTON executed loan agreements with the same financial institution, and signed one or more documents by which he agreed to be personally liable for repayment of those loans, which totaled more than \$9 million. BOLTON’s 2000 CDS transaction generated for him a tax deduction of approximately \$14.9 million. He used that deduction to offset his 2000 income.

85. In late 2001, defendant CHARLES BOLTON again caused BIG Trading Partners to enter two swaps with a financial institution. As structured, those swaps were designed to generate a business deduction for BOLTON of approximately \$25 million in 2001. As part of the 2001 CDS transaction, BOLTON executed another loan agreement with the same financial institution, and signed one or more documents by which he agreed to be personally liable for repayment of that loan, which was in the amount of approximately \$21 million. During a period of approximately seventeen days in 2001, BOLTON’s second CDS transaction generated for him a tax deduction of approximately \$24.9 million. He used that deduction to offset his 2001 income.

86. In connection with his own two CDS transactions, defendant CHARLES BOLTON signed representation letters, prepared by Law Firm A, in which he falsely stated, among other things, that he regarded the various investments of the Partnership – including the

swaps and the trading activities – as comprising one coherent business philosophy,” and that this diversity of investments was “an important element in [his] decision to invest in the Partnership.”

87. In support of each of his two tax shelters, defendant CHARLES BOLTON obtained a legal opinion from Law Firm A. Each opinion falsely stated, among other things, that “a significant purpose of [BOLTON’s] investment in the Partnership [was] to obtain a profit through access to the specialized investment strategies and activities offered by the Partnership. According to one of the two letters, such investments and activities were not otherwise readily available to BOLTON.

88. Defendant CHARLES BOLTON was audited by the IRS. In connection with that audit, he submitted the two legal opinions.

89. On or about April 13, 2005, in connection with his own CDS transactions, defendant CHARLES BOLTON gave sworn testimony to the IRS. On that occasion, BOLTON falsely testified, among other things, that the decision to terminate his 2000 swap at the early termination date was made for economic reasons, and that he was not aware his own swap had to terminate early in order for him to derive the tax benefits.

90. On or about July 28, 2006, the IRS notified BOLTON that it intended to assert penalties against BOLTON for claiming losses from CDS on his 2000 and 2001 tax returns. In its notification letter, the IRS informed BOLTON of its view that “a significant purpose” of BOLTON’s CDS transactions was tax avoidance. In response, BOLTON submitted a statement, signed under penalties of perjury, in which he stated that the IRS was incorrect in asserting that a “significant purpose” of his CDS transactions was tax avoidance, and that his decision was “primarily profit driven.”

Statutory Allegations

91. From in or about early 1998 through in or about 2006, in the Southern District of New York and elsewhere, ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, DAVID L. SMITH and CHARLES BOLTON, the defendants, together and with each other and with others known and unknown, unlawfully, willfully and knowingly did combine, conspire, confederate and agree to defraud the United States and an agency thereof, to wit, the Internal Revenue Service (“IRS”) of the United States Department of Treasury, and to commit offenses against the United States, to wit, violations of Title 26, United States Code, Section 7201, and Title 18, United States Code, Section 1001.

92. It was a part and an object of the conspiracy that ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, DAVID L. SMITH and CHARLES BOLTON, the defendants, and their co-conspirators, unlawfully, wilfully and knowingly would and did defraud the United States and the IRS by impeding, impairing, defeating and obstructing the lawful governmental functions of the IRS in the ascertainment, evaluation, assessment, and collection of income taxes.

93. It was a part and an object of the conspiracy that ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, DAVID L. SMITH and CHARLES BOLTON, the defendants, and their co-conspirators, unlawfully, wilfully and knowingly would and did attempt to evade and defeat a substantial part of the income taxes due and owing to the United States by E&Y’s Add-On clients, in violation of Title 26, United States Code, Section 7201.

94. It was a part and an object of the conspiracy that ROBERT COPLAN, MARTIN NISSENBAUM, and RICHARD SHAPIRO, the defendants, and their co-conspirators, unlawfully, wilfully and knowingly would and did attempt to evade and defeat a substantial part of the income taxes due and owing to the United States by themselves and other E&Y partners, in violation of Title 26, United States Code, Section 7201.

95. It was a part and an object of the conspiracy that ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, DAVID L. SMITH and CHARLES BOLTON, the defendants, and their co-conspirators, unlawfully, wilfully and knowingly would and did make materially false, fictitious, and fraudulent statements and representations in matters within the jurisdiction of the executive branch of the Government of the United States, in violation of Title 18, United States Code, Section 1001.

Means and Methods of the Conspiracy

96. Among the means and methods by which ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, DAVID L. SMITH and CHARLES BOLTON, the defendants, and their co-conspirators, would and did carry out the objectives of the conspiracy were the following:

a) They would and did design, market and implement tax shelter transactions, and create false and fraudulent factual scenarios to support those transactions, so that wealthy individuals could pay a percentage of their income or gain in fees to E&Y, PCMG, the Bolton companies, and the other participants in the transactions, rather than paying a substantially greater amount in taxes to the IRS;

b) They would and did design, market and implement tax shelter transactions in ways that made them difficult for the IRS to detect;

c) They would and did design, market and implement tax shelter transactions in ways that disguised the fact that the shelters were largely or exclusively tax-motivated, and lacked substantial non-tax business purposes;

d) They would and did seek to prevent the IRS from learning that they had marketed strategies consisting of pre-planned steps leading to pre-determined tax benefits;

e) They would and did prepare and assist in preparing false and fraudulent documents to deceive the IRS, including but not limited to, engagement letters, transactional documents, representation letters, and correspondence;

f) They would and did assist in crafting legal opinions designed to shield E&Y's clients from penalties, knowing that these opinions contained false, fraudulent and misleading information and omitted other information, all of which was material to a determination of whether the tax results claimed by the clients were allowable;

g) They would and did prepare and cause to be prepared tax returns that were false and fraudulent because, among other things, they incorporated phony tax losses and thereby substantially understated the tax due and owing by the shelter clients;

h) They would and did destroy documents and take other steps to prevent the creation and retention of materials that would reveal to the IRS the true facts surrounding the fraudulent tax shelters;

i) they would and did provide false, fraudulent and misleading information in response to IDRs issued by the IRS in connection with audits of tax shelter

transactions;

j) they would and did draft documents to be submitted by the tax shelter clients to the IRS in connection with the IRS's voluntary disclosure initiative, under penalties of perjury, which they knew contained false statements of material fact and omitted material facts; and

k) they would and did make false and misleading statements, under oath, in connection with efforts by the IRS to ascertain the circumstances surrounding the design, marketing and implementation of the tax shelters.

OVERT ACTS

97. In furtherance of the conspiracy and to effect the illegal objects thereof, ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, DAVID L. SMITH and CHARLES BOLTON, the defendants, and their co-conspirators, committed the following overt acts, among others, in the Southern District of New York and elsewhere:

a) In or about late 1998 or early 1999, defendant DAVID L. SMITH explained CDS to the E&Y defendants.

b) In or about early 1999, defendants ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN and DAVID L. SMITH discussed conducting "box trades" in the CDS trading accounts.

c) In or about early 1999, defendants BRIAN VAUGHN and DAVID SMITH described CDS to potential clients.

d) In or about mid-1999, defendant DAVID L. SMITH discussed CDS with defendant CHARLES BOLTON;

e) In or about November 1999, the E&Y defendants created and distributed a “COBRA Action Plan” to PFC personnel, which instructed, “**DO NOT** leave marketing materials with client under any circumstances,” and which further instructed, “**DO NOT** reference tax losses in the engagement letter.”

f) On or about December 5, 1999, defendant ROBERT COPLAN sent an email to PFC personnel whose COBRA clients had option positions that were “in the money,” warning that if the clients cashed out of those positions at too large a discount, they would undermine their tax argument, which was based upon the chance of making a profit in excess of fees.

g) In or about early February 2000, defendant CHARLES BOLTON agreed that Bolton Asset Management, LLC (“BAM”) would license CDS from defendant DAVID L. SMITH, and would pay SMITH royalties based on the net fees generated.

h) On or about February 8, 2000, defendant RICHARD SHAPIRO sent an email to defendants ROBERT COPLAN, MARTIN NISSENBAUM and BRIAN VAUGHN, offering to be involved in CDS sales contacts.

i) On or about February 8, 2000, after reviewing a proposed “CDS Action Plan,” defendant RICHARD SHAPIRO sent an email to defendants ROBERT COPLAN, MARTIN NISSENBAUM, and BRIAN VAUGHN, among others, expressing his concern about the existence of a document which laid out in writing “all the chapters and verses” of CDS, and which indicated “before the fact” that the swaps would terminate early.

j) In or about early 2000, the defendants created and distributed a “CDS Action Plan” to PFC personnel which instructed, “**DO NOT** leave marketing materials with client under any circumstances,” and which further instructed, “**DO NOT** reference tax losses in the engagement letter.”

k) On or about February 18, 2000, Belle Six, a co-conspirator not named as a defendant herein, sent an email concerning an economic model prepared for a CDS transaction, stating, “[I]n meeting with the E&Y people on Tuesday, we have a list of things that we would like you to change on the model. . . . We don’t want to highlight that we don’t anticipate trading profits. Please remove it from the economic model.”

l) On or about April 14, 2000, defendant RICHARD SHAPIRO told defendants ROBERT COPLAN, MARTIN SHAPIRO, and BRIAN VAUGHN in an email that it was “essential” to delete from a CDS economic model a footnote stating that the calculations set forth in the model assumed early termination of the swap.

m) On or about April 21, 2000, in response to concerns expressed by a PFC practice member that CDS could result in a complete loss of the CDS partnership’s capital, thereby exposing the client to personal liability, Belle Six, a co-conspirator not named as a defendant herein explained, “In reality, even if the client loses everything they will not have to contribute any more money.”

n) In or about early May 2000, in an Instant Message (“IM”) conversation between defendant BRIAN VAUGHN and defendant ROBERT COPLAN, VAUGHN told COPLAN about an idea to combine the CDS strategy with the COBRA strategy.

o) On or about May 5, 2000, defendant ROBERT COPLAN forwarded his IM conversation with defendant BRIAN VAUGHN to defendants MARTIN NISSENBAUM and RICHARD SHAPIRO.

p) On or about June 5, 2000, defendant ROBERT COPLAN sent an email to PFC practice members, announcing the availability of the CDS Add-On strategy, in which he described it as an “indefinite capital gain deferral strategy.”

q) On or about June 14, 2000, defendant ROBERT COPLAN sent an email to PFC professionals, explaining that if PowerPoint slides setting out the steps of CDS Add-On “ever made their way to the IRS . . . the entire business purpose argument that [gave] us the ability to distinguish this from COBRA would be out the window.”

r) On or about July 10, 2000, defendant ROBERT COPLAN drafted a letter to be sent by E&Y to prospective CDS Add-On clients, in which he described the Add-On strategy as a consolidation of a portion of the client’s trading account “to further diversify the trading and enhance performance.”

s) On or about July 20, 2000, a co-conspirator not named as a defendant herein who was employed by the Bolton companies sent an email to defendant CHARLES BOLTON and others, explaining that due to the limited volume of trading being done by traders for the CDS portfolios, it was necessary to consider allocating a portion of the portfolios to a trader who had lost money previously.

t) In or about June or July 2000, defendant DAVID L. SMITH signed letters to E&Y’s 1999 CDS clients, advising them that “in an effort to diversify trading returns and enhance performance,” PCMG was considering the possibility of trading in digital currency

options, and stating that once such trading had begun, PCMG would “consider whether the [client’s CDS partnership] should consolidate its trading account into a single entity with the trading accounts of others . . . , in order to further enhance returns by utilizing economies of scale, reducing administrative costs, and simplifying the trading structure.”

u) In or about mid- to late July 2000, defendants DAVID L. SMITH and CHARLES BOLTON signed three agreements under which BCP took over PCMG’s role as the general partner for the 1999 CDS partnerships that were planning to participate in the Add-On shelter.

v) On or about August 4, 2000, defendant ROBERT COPLAN sent an email to defendants MARTIN NISSENBAUM, RICHARD SHAPIRO and BRIAN VAUGHN, as well as to PFC practice members, in which he explained that a loan amendment document would highlight for the IRS the issue of whether the CDS clients had personal liability on their CDS loans, and advised them “to dispose of the loan amendment document after you have reviewed it.”

w) On or about August 9, 2000, pursuant to an agreement to pay defendant BRIAN VAUGHN for his role in providing tax shelter clients, defendant CHARLES BOLTON directed that \$1 million be transferred to another account, purportedly for the purchase of a copyright on a song composed by VAUGHN.

x) From in or about August 2000 through November 2000, defendant CHARLES BOLTON directed the payment of approximately \$3.75 million to defendant DAVID L. SMITH, pursuant to the CDS licensing agreement.

y) In or about September 2000, defendant DAVID L. SMITH signed a letter notifying the bank that served as the counter-party to the 1999 CDS transactions that several CDS partnerships wished to terminate their swaps at the early termination date.

z) On or about September 20, 2000, in an effort to increase the total value of trades in the CDS trading accounts, approved hiring a trading firm without a significant track record that was willing to create trades for the Bolton companies that involved low risk and low returns.

aa) On or about October 25, 2000, defendant CHARLES BOLTON formed BIG Trading Partners, L.P.

bb) On or about October 28, 2000, defendant CHARLES BOLTON caused BIG Trading Partners to enter into two swaps and two loan agreements with a financial institution.

cc) On or about November 27, 2000, defendant ROBERT COPLAN sent an email to another PFC professional, with a copy to defendants RICHARD SHAPIRO and BRIAN VAUGHN, explaining that SISG did not leave with clients promotional materials that went through the steps of a strategy, or that highlighted the benefits of a strategy, because “the less evidence there is that the client responded to a tax-savings promotion, the better his argument that there were non-tax motivations guiding his actions.”

dd) On or about November 20, 2000, defendant ROBERT COPLAN sent an email to E&Y personnel whose clients had implemented Add-On transactions, explaining the purpose of the “second round of digital options” letter.

ee) In or about 2000 and 2001, defendant MARTIN NISSENBAUM participated in presenting the CDS strategy to clients.

ff) In or about 2000 and 2001, defendant MARTIN NISSENBAUM participated in presenting the PICO strategy to clients.

gg) In or about late 2000, defendants ROBERT COPLAN, MARTIN NISSENBAUM and RICHARD SHAPIRO signed the Tradehill Operating Agreement and the Churchwind Operating Agreement.

hh) In or about November 2000, defendant MARTIN NISSENBAUM caused the contribution of Churchwind to ADFX.

ii) On or about January 22, 2001, in connection with the registration of CDS as a tax shelter, defendant CHARLES BOLTON submitted to the IRS a document entitled "Description of the Transaction Registered by Bolton," which stated, "If the general partner, based on market fluctuations, terminates the swap contracts early, capital gain would arise on such termination."

jj) On or about February 7, 2001, defendant ROBERT COPLAN sent an email to the defendants and to other PFC personnel, explaining that assets placed in the PICO LLC's trading account should be used for trading, and that this needed to be addressed with clients who had "different ideas."

kk) On or about April 15, 2001, defendant ROBERT COPLAN filed his Form 1040 for the year 2000, on which he reported losses he had generated through the Tradehill transaction.

ll) On or about April 16, 2001, defendant MARTIN NISSENBAUM filed his Form 1040 for the year 2000, on which he reported losses he had generated through the Tradehill transaction.

mm) On or about May 17, 2001, defendant RICHARD SHAPIRO discussed COBRA with representatives of the IRS in connection with the audit of three COBRA clients.

nn) On or after May 9, 2001, defendant ROBERT COPLAN signed a consulting agreement between E&Y and an affiliate of Company Z, which was backdated to January 3, 2001.

oo) On or about May 22, 2001, defendant RICHARD SHAPIRO sent an email cautioning against leaving presentation materials with clients, explaining that in the Minneapolis COBRA audit, the taxpayer had been asked to produce promotional materials.

pp) On or about May 24, 2001, defendant ROBERT COPLAN sent an email to defendants MARTIN NISSENBAUM and RICHARD SHAPIRO, as well as others, recommending that the CDS partnerships maintain their trading activity through the end of the year in which the CDS swaps terminated, in order to avoid raising an issue with the IRS about whether the CDS partnerships were actually engaged in a trade or business.

qq) On or about June 6, 2001, defendant ROBERT COPLAN asked Belle Six, a co-conspirator not named as a defendant herein, to consider changing the names of the CDS partnerships so that it would be more difficult for the IRS to identify all the CDS transactions.

rr) On or about June 28, 2001, defendant BRIAN VAUGHN sent an email to a co-conspirator, stating with respect to a CDS transaction, “We should consider removing the footnote language concerning implied early termination. This could adversely affect our tax situation given the level of audits that are currently in progress. . . . Remember our goal is to convince the agents the client did not have a predisposition of early termination.”

ss) On or about July 12, 2001, defendant ROBERT COPLAN sent an email directing that clients who had already implemented PICO transactions be given a brochure describing PICO, and explaining that the brochure conveyed information necessary “for the client to have made [an] informed decision” to embark on the PICO transaction.

tt) On or about July 17, 2001, defendant ROBERT COPLAN sent an email directing the recipients immediately to “delete and dispose of” COBRA materials in their files and their computers.

uu) On or about August 16, 2001, defendant RICHARD SHAPIRO filed his Form 1040 for the year 2000, on which he reported losses he had generated through the Tradehill transaction.

vv) On or about September 14, 2001, defendant ROBERT COPLAN emailed a form letter to E&Y personnel whose CDS clients might wish to close down their trading accounts, suggesting that the clients use the form letter – which attributed their desire to end their trading activity to the September 11th terrorist attacks – to “document for the file a logical non-tax rationale.”

ww) On or about October 15, 2001, defendant CHARLES BOLTON filed his Form 1040, for calendar year 2000, on which he claimed a loss of \$14,919,583 from

participating in a CDS transaction through BIG Trading Partners.

xx) On or about October 31, 2001, in response to an email from defendant ROBERT COPLAN inquiring about how to respond to an IDR sent by the IRS in connection with a COBRA audit, defendant MARTIN NISSENBAUM stated, "Never give them more than they ask for. (That's why we never allow clients to attend examinations, they talk too much)."

yy) On or about November 12, 2001, defendant ROBERT COPLAN emailed defendants MARTIN NISSENBAUM and RICHARD SHAPIRO, informing them, "Bolton is suggesting that the [CDS] partnerships be shut down after essentially 13.5 months," and asking, "Should we intercede and suggest running another year out with the trading account?"

zz) On or about November 12, 2001, defendant MARTIN NISSENBAUM responded to the email sent by defendant ROBERT COPLAN earlier that day, stating, "Yes. They sound way too anxious to get out."

aaa) On or about November 12, 2001, defendant RICHARD SHAPIRO responded to the two emails sent by defendants ROBERT COPLAN and MARTIN NISSENBAUM earlier that day, stating, "I AGREE WITH MARTIN."

bbb) On or about November 26, 2001, defendant ROBERT COPLAN sent an email to an E&Y employee, discouraging the use of a document that described SISG's strategies and their accompanying tax benefits, explaining that such documents would provide evidence of their clients' tax avoidance motives, and that SISG's "ultimate goal" was "to make our strategies appear to be investment techniques that have advantageous tax consequences."

ccc) On or about December 14, 2001, defendant CHARLES BOLTON caused BIG Trading Partners to enter into two swaps and two loan agreements with a financial institution.

ddd) In or about February and March 2002, defendants ROBERT COPLAN, MARTIN NISSENBAUM and RICHARD SHAPIRO drafted and reviewed template disclosure documents that would be used by clients who wished to participate in an amnesty program announced by the IRS.

eee) On or about June 12, 2002, defendant BRIAN VAUGHN gave false and misleading testimony to the IRS.

fff) On or about June 20, 2002, defendant ROBERT COPLAN gave false and misleading testimony to the IRS.

ggg) On or about October 15, 2002, defendant CHARLES BOLTON filed his Form1040 for calendar year 2001, on which he claimed a loss of \$24,994,225 from participating in a CDS transaction through BIG Trading Partners.

hhh) In or about September 2003, defendant MARTIN NISSENBAUM provided false and misleading information to an individual who was preparing responses to IDRs sent by the IRS to the eleven E&Y partners who had participated in the Tradehill transaction.

iii) On or about December 9, 2003, defendant DAVID L. SMITH provided false and misleading testimony to the IRS.

jjj) On or about April 12 and 13, 2005, defendant CHARLES BOLTON provided false and misleading testimony to the IRS.

kkk) On or about August 18, 2006, defendant CHARLES BOLTON signed a document under penalties of perjury, stating that his participation in his CDS transactions was “primarily profit driven,” and that tax avoidance was not a “significant purpose.”

(Title 18, United States Code, Section 371).

COUNT TWO

(Tax Evasion of The L. Trading Group)

The Grand Jury further charges:

98. The allegations set forth in paragraphs 1 through 10, 12 through 18, 27 through 53, 60 through 67, 96 and 97 are repeated and realleged as if fully set forth herein.

99. Among the entities that participated in the Add-On tax shelter without first having done a CDS shelter was a trading group referred to herein as the “L. Trading Group.” The L. Trading Group was a company whose two members were involved in options trading. In July 2000, E&Y personnel met with representatives of the L. Trading Group and offered the L. Trading Group the opportunity to defer indefinitely the tax liability of the company’s members on income earned in 2000. The two L. Trading Group members decided to use the Add-On strategy to generate a tax loss of \$30 million. Because the L. Trading Group was a “pass-through” entity for tax purposes, that tax loss could be used by the members to offset their individual income for 2000.

100. On or about August 3, 2000, the Bolton companies arranged for the L. Trading Group to acquire three pairs of digital currency options. The premiums on the three long

options totaled approximately \$30 million. The cost to the L. Trading Group of the three option pairs (the “net premium”) was approximately \$150,000, and the maturity date was November 3, 2000. The option pairs were structured with a 30% probability of a 2:1 return. Thus, if at maturity all three option pairs were “in the money” – which was statistically unlikely – the L. Trading Group would receive a payout of approximately \$300,000, representing a return of the group’s original contribution, plus a profit of approximately \$150,000. However, the fees charged in connection with the transaction included a \$375,000 fee to E&Y, a \$375,000 fee to the Bolton companies, and a \$75,000 fee payable to Law Firm A for a legal opinion. Accordingly, the L. Trading Group had no realistic possibility to make a profit.

101. On or about August 8, 2000, the L. Trading Group’s option pairs were transferred to BCPT&I in accordance with the pre-planned series of steps constituting the Add-On transaction. On or about November 3, 2000, representatives of L. Trading Group signed a letter indicating that the L. Trading Group did not wish to participate in “a second round of digital option purchases.” Accordingly, in or about December 2000, the L. Trading Group withdrew from BCPT&I, and BCPT&I distributed Japanese yen valued at approximately \$21,000 to the L. Trading Group. The L. Trading Group exchanged the yen and claimed a tax loss of approximately \$30 million, which loss flowed through to the individual tax returns filed by the members of the L. Trading Group.

102. In or about April 2002, at the behest of E&Y, the managing member of the L. Trading Group signed a representation letter that had been drafted by Law Firm A. That letter contained false and misleading representations, including representations that “[t]he Company regularly engage[d] in investments similar in opportunity and risk to those presented by the digital foreign currency options,” and that “Company management reasonably anticipated a pre-

tax profit” on the transaction. Shortly thereafter, upon payment of a \$75,000 fee, Law Firm A issued a legal opinion that incorporated the false and misleading statements contained in the representation letter, as well as the false and misleading “cover story” that had been created in 2000 to provide a purported business purpose for the Add On transaction. The opinion letter also stated that the L. Trading Group’s digital currency options could have returned 200 times the amount contributed by the L. Trading Group (200 x \$150,000, or \$30 million), and that “[t]he potential for such a large payout was an important factor in the Company’s analysis of the option trades.” In reality, a \$30 million payout on the option pairs – while hypothetically possible – was virtually impossible as a practical matter, and the hypothetical possibility of such a payout played no role whatsoever in the decision by the members of the L. Trading Group to implement the Add-On tax shelter.

103. In or about early 2002, after the IRS announced its voluntary disclosure initiative, the two members of the L. Trading Group elected to participate. On or about April 22, 2002, they signed letters that had been prepared by E&Y, in order to disclose their Add-On transaction to the IRS (the “amnesty letters”). Those amnesty letters, which were signed under penalties of perjury by each taxpayer and his spouse, were submitted to the IRS, and contained various false and misleading statements. Among other things, the amnesty letters reiterated the false “cover story” developed by the conspirators in 2000. The amnesty letters also included the false statements that the business objective of BCPT&I was capital appreciation; that the management of the L. Trading Group “was familiar with [digital] options, and in particular, the opportunity for significant economic returns in proportion to the funds invested”; and that each taxpayer and his spouse “firmly believe[d] that [their] business purpose for this transaction was

sound and remain[ed] sound.”

104. On August 26, 2003, a representative of the L. Trading Group appeared before the IRS to provide sworn testimony concerning the company’s Add-On transaction. During that proceeding, the representative of L. Trading Group gave false, misleading and evasive testimony in order to conceal a number of facts from the IRS, including the fact that the transaction was tax-motivated.

Statutory Allegations

105. From in or about January 1, 2000, through at least in or about 2003, in the Southern District of New York and elsewhere, ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, and CHARLES BOLTON, the defendants, unlawfully, wilfully and knowingly did aid, abet, counsel, induce and procure an attempt to evade and defeat a substantial part of the income tax due and owing by the members of the L. Trading Group to the United States of America for calendar year 2000, by various means, including among others:

- a) designing and implementing a tax shelter transaction which they knew had no reasonable possibility of generating a profit;
- b) using that tax shelter to generate a total of approximately \$30 million in tax losses which they knew could not properly be deducted on the returns of the L. Trading Group members;
- c) creating an entity (BCPT&I) that served no legitimate business purpose, but was used merely to obtain tax benefits for clients as well as fees for E&Y, the Bolton companies, Law Firm A and others;

d) causing to be prepared, and causing to be signed and filed, false and fraudulent U.S. Individual Income Tax Returns, Forms 1040, for calendar year 2000, which understated each member's taxable income and the tax due and owing thereon; and

e) preparing, executing, and causing the execution of false and fraudulent documents intended to deceive the IRS, including applications for participation in the IRS's voluntary disclosure initiative.

(Title 26, United States Code, Section 7201 and
Title 18, United States Code, Section 2)

COUNT THREE

(Tax Evasion of The C. Partnership)

The Grand Jury further charges:

106. The allegations set forth in paragraphs 1 through 10, 12 through 18, 27 through 53, 60 through 67, 96 and 97 are repeated and realleged as if fully set forth herein.

107. Among the entities that participated in the Add-On tax shelter without first having done a CDS shelter was a trading group referred to herein as the "C. Partnership." The C. Partnership consisted of seven partners, most of whom were involved in options trading. In July 2000, E&Y personnel met with representatives of the C. Partnership and offered the partnership the opportunity to defer indefinitely the tax liability of the individual partners on income earned in 2000. The partners decided to use the Add-On strategy to generate a tax loss of \$20 million. Because the C. Partnership was a "pass-through" entity for tax purposes, that tax loss could be used by the partners to offset their individual income for 2000.

108. On or about August 9, 2000, the Bolton companies arranged for the C. Partnership to acquire two pairs of digital currency options. The premiums on the two long options totaled approximately \$20 million. The cost to the C. Partnership of the two option pairs (the “net premium”) was approximately \$100,000, and the maturity date was December 7, 2000. The option pairs were structured with a 30% probability of a 2:1 return. Thus, if at maturity both option pairs were “in the money” – which was statistically unlikely – the C. Partnership would receive a payout of approximately \$200,000, representing a return of the group’s original contribution, plus a profit of approximately \$100,000. However, the fees charged in connection with the transaction included a \$225,000 fee to E&Y, a \$250,000 fee to the Bolton companies, and a \$75,000 fee payable to Law Firm A for a legal opinion. Accordingly, the C. Partnership had no realistic possibility to make a profit.

109. On or about August 11, 2000, the C. Partnership’s option pairs were transferred to BCPT&I in accordance with the pre-planned series of steps constituting the Add-On transaction. On or about November 3, 2000, a representative of C. Partnership signed a letter indicating that the partnership did not wish to participate in “a second round of digital option purchases.” Accordingly, in or about December 2000, the C. Partnership withdrew from BCPT&I, and BCPT&I distributed Japanese yen worth approximately \$14,000 to the C. Partnership. The C. Partnership sold that asset and claimed a tax loss of approximately \$20 million. That loss flowed through to the individual tax returns filed by the partners of C. Partnership for 2000.

110. In or about early 2002, after the IRS announced its voluntary disclosure initiative, the C. Partnership partners elected to participate. On or about April 22, 2002, they signed letters that had been prepared by E&Y, in order to disclose their Add-On transaction to

the IRS (the “amnesty letters”). Those amnesty letters, which were signed under penalties of perjury by each taxpayer and his spouse, were submitted to the IRS, and contained various false and misleading statements. Among other things, the amnesty letters reiterated the false “cover story” developed by the conspirators in 2000. The amnesty letters also included the false statements that the business objective of BCPT&I was capital appreciation; that C. Partnership’s management “was familiar with [digital] options, and in particular, the opportunity for significant economic returns in proportion to the funds invested”; and that each taxpayer and his spouse “firmly believe[d] that [their] business purpose for this transaction was sound and remain[ed] sound.”

111. In or about mid-2002, after the partners had already decided to participate in the voluntary disclosure program, Law Firm A sent to the C. Partnership a representation letter to be signed by one of the partners, a draft legal opinion, and a bill for \$75,000. The representation letter contained false and misleading representations, including representations that “[t]he Partnership regularly engage[d] in investments similar in opportunity and risk to those presented by the digital foreign currency options,” and that “Partnership management reasonably anticipated a pre-tax profit” on the transaction. The draft legal opinion incorporated the false and misleading statements contained in the representation letter, as well as the false and misleading “cover story” that had been created in 2000 to provide a purported business purpose for the Add On transaction. The draft opinion letter also stated that the C. Partnership’s digital currency options could have returned 200 times the amount contributed by the C. Partnership (200 x \$100,000, or \$20 million), and that “[t]he potential for such a large payout was an important factor in the Company’s analysis of the option trades.” In reality, a \$20 million payout on the

option pairs – while hypothetically possible – was virtually impossible as a practical matter, and the hypothetical possibility of such a payout played no role whatsoever in the decision by the partners of the C. Partnership to implement the Add-On tax shelter. Because the partners had already decided to participate in the voluntary disclosure initiative, they did not pay for, or obtain, a final legal opinion from Law Firm A.

112. On December 15, 2003, one of the partners of the C. Partnership appeared before the IRS to provide sworn testimony concerning the partnership's Add-On transaction. During that proceeding, the partner gave false, misleading and evasive testimony in order to conceal a number of facts from the IRS, including the fact that the transaction was tax-motivated.

Statutory Allegations

113. From in or about January 1, 2000, through at least in or about 2003, in the Southern District of New York and elsewhere, ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, and CHARLES BOLTON, the defendants, unlawfully, wilfully and knowingly did aid, abet, counsel, induce and procure an attempt to evade and defeat a substantial part of the income tax due and owing by the partners of the C. Partnership to the United States of America for calendar year 2000, by various means, including among others:

- a) designing and implementing a tax shelter transaction which they knew had no reasonable possibility of generating a profit;
- b) using that tax shelter to generate a total of approximately \$20 million in tax losses which they knew could not properly be deducted on the returns of the C.

Partnership partners;

c) creating an entity (BCPT&I) that served no legitimate business purpose, but was used merely to obtain tax benefits for clients as well as fees for E&Y, the Bolton companies, Law Firm A and others;

d) causing to be prepared, and causing to be signed and filed false and fraudulent U.S. Individual Income Tax Returns, Forms 1040, for calendar year 2000, which understated each partner's taxable income and the tax due and owing thereon; and

e) preparing, executing, and causing the execution of false and fraudulent documents intended to deceive the IRS, including applications for participation in the IRS's voluntary disclosure initiative.

(Title 26, United States Code, Section 7201 and
Title 18, United States Code, Section 2)

COUNT FOUR

(Tax Evasion of T.M. and K.M.)

The Grand Jury further charges:

114. The allegations set forth in paragraphs 1 through 10, 12 through 18, 27 through 53, 60 through 67, 96 and 97 are repeated and realleged as if fully set forth herein.

115. Among the E&Y clients who participated in a CDS tax shelter as well as the Add-On tax shelter were T.M. and K.M., a married couple.

116. In 2000, T.M. held stock options in his company. Under the tax law, if T.M. elected to exercise those stock options, he would incur an immediate tax liability on the

difference between his purchase price and the fair market value of the stock on the exercise date. In addition, if he exercised the options, he would be prohibited from selling the stock for a significant period of time, and thus would not be able to sell stock in order to satisfy his tax obligation.

117. In or about July 2000, K.M. spoke with a representative of E&Y, and learned that if T.M. exercised the stock options, he could use CDS to defer the tax liability on the stock purchase to 2001, and convert the tax rate to the capital gains rate. K.M. learned that if T.M. also implemented CDS Add-On, he could further defer the tax liability beyond 2001. Thus, as explained by E&Y, by implementing these shelters, T.M. and K.M. could defer their tax liability until such time as they could sell the stock, and pay their tax at a lower rate.

118. Based on E&Y's advice, T.M. exercised his stock options, and T.M. and K.M. implemented both CDS and CDS Add-On, in order to reduce and defer to a future year their tax liability on approximately \$20 million in income. On or about July 28, 2000, they formed a CDS partnership, M. Trading Partners, L.P. ("M. Trading Partners"), with BCP as its general partner. As planned, M. Trading Partners entered into two swaps and a loan with a financial institution, and engaged in trading activity designed to secure "trader" status for the partnership.

119. On or about August 8, 2000, the Bolton companies arranged for M. Trading Partners to acquire two pairs of digital currency options. The premiums on the two long options totaled approximately \$20 million. The cost to M. Trading Partners of the two option pairs (the "net premium") was approximately \$100,000, and the maturity date was December 7, 2000. The option pairs were structured with a 30% probability of a 2:1 return. Thus, if at

maturity both option pairs were “in the money” – which was statistically unlikely – M. Trading Partners would receive a payout of approximately \$200,000, representing a return of their original contribution, plus a profit of approximately \$100,000. However, fees charged in connection with the transaction included a \$150,000 fee to E&Y, a \$150,000 fee to the Bolton companies, and a \$75,000 fee payable to Law Firm A for a legal opinion. Accordingly, M. Trading Partners had no realistic possibility to make a profit on the Add-On transaction.

120. On or about August 11, 2000, M. Trading Partners’ option pairs were transferred to BCPT&I in accordance with the pre-planned series of steps constituting the Add-On transaction. T.M. and K.M. were sent a “second round of digital option trading” letter, but did not sign it, thereby indicating that they would retain their membership in BCPT&I into 2001. In 2001, M. Trading Partners withdrew from BCPT&I, and BCPT&I distributed Japanese yen to the partnership. M. Trading Partners sold that asset and claimed a tax loss of approximately \$20 million, which flowed through to the individual tax return they filed for 2001. In order for T.M. and K.M. to use the tax losses generated through the Add-On transaction, defendant CHARLES BOLTON signed a loan agreement on behalf of L. Trading Partners, by which the partnership purported to borrow \$8.5 million from a financial institution. On the same day, T.M. and K.M. signed documents by which they agreed to be personally liable for the repayment of that loan.

121. On September 25, 2001, at the behest of E&Y, T.M. and K.M. each signed a representation letter that had been drafted by Law Firm A in connection with the CDS Add-On shelter. The letters contained false and misleading representations, including representations that they regarded the various activities of their CDS partnership, “including the

swaps, the trading activities, loan, and the investment in [BCPT&I], as comprising one coherent business philosophy,” and that “this diversity of investments was an important element in [their] decision to invest in the Partnership[.]”

122. On September 24, 2001, defendant CHARLES BOLTON also signed a representation letter in connection with the Add-On transaction implemented by T.M. and K.M. That letter falsely stated, among other things, that BOLTON intended to utilize the funds supposedly loaned to M. Trading Partners “as appropriate, to leverage the existing trading programs of the Partnership and/or invest in other programs designed to yield returns in excess of the cost of the funds while minimizing risk to capital[.]”

123. In exchange for a fee of \$75,000, Law Firm A issued a legal opinion that incorporated the false and misleading statements contained in the representation letters signed by T.M. and K.M., as well as the false and misleading “cover story” that had been created in 2000 to provide a purported business purpose for the Add On transaction. The opinion letter also stated that M. Trading Partners’ digital currency options had a potential payout of “many times the amount of the net premium,” and that “[t]he potential for a large payout was an important factor in the partners’ interest in the option trades.” In reality, a payout of “many times the amount of the net premium” – while hypothetically possible – was virtually impossible as a practical matter, and the hypothetical possibility of such a payout played no role whatsoever in the decision by T.M. and K.M. to implement the Add-On tax shelter. The opinion letter also falsely stated that the Add-On loan taken out by M. Trading Partners would be used “to opportunistically invest” in trading programs, and would therefore be deemed a genuine loan for tax purposes.

124. In or about early 2002, after the IRS announced its voluntary disclosure initiative, T.M. and K.M. elected to participate. On or about March 13, 2002, they signed a letter that had been prepared by E&Y, in order to disclose their Add-On transaction to the IRS (the “amnesty letter”). The amnesty letter, which was signed under penalties of perjury by T.M. and K.M., was submitted to the IRS, and contained various false and misleading statements. Among other things, the amnesty letter reiterated the false “cover story” developed by the conspirators in 2000, and asserted that the business objective of BCPT&I was to accomplish asset appreciation.

Statutory Allegations

125. From in or about January 1, 2000 through at least in or about April 2002, in the Southern District of New York and elsewhere, ROBERT COPLAN, MARTIN NISSENBAUM, RICHARD SHAPIRO, BRIAN VAUGHN, and CHARLES BOLTON, the defendants, unlawfully, wilfully and knowingly did aid, abet, counsel, induce and procure an attempt to evade and defeat a substantial part of the income tax due and owing by T.M. and K.M. to the United States of America for calendar year 2001 by various means, including among others:

- a) designing and implementing a CDS Add-On tax shelter transaction which they knew had no reasonable possibility of generating a profit;
- b) using that tax shelter to generate more than \$19 million in tax losses they knew could not properly be deducted on the returns of the partners;
- c) creating an entity (BCPT&I) that served no legitimate business purpose, but was used merely to obtain tax benefits;

d) causing to be prepared, and causing to be signed and filed, a false and fraudulent U.S. Individual Income Tax Return, Form 1040, for calendar year 2001, which substantially understated T.M. and K.M.'s taxable income and the tax due and owing;

e) preparing, executing, and causing the execution of false and fraudulent documents intended to deceive the IRS, including applications for participation in the IRS's voluntary disclosure initiative; and

f) taking various other steps to conceal from the IRS the true facts relating to the tax shelter, including providing false information in response to IDRs.

(Title 26, United States Code, Section 7201 and
Title 18, United States Code, Section 2)

COUNTS FIVE THROUGH SEVEN

(Tax Evasion of E&Y Partners)

The Grand Jury further charges:

126. The allegations set forth in paragraphs 1 through 10, 13 through 20, 27 through 34, 68 through 82, 96 and 97 are repeated and realleged as if fully set forth herein.

127. From in or about 2000, through at least in or about 2003, in the Southern District of New York and elsewhere, ROBERT COPLAN, MARTIN NISSENBAUM, and RICHARD SHAPIRO, the defendants, unlawfully, wilfully and knowingly did attempt to evade and defeat a substantial part of the income tax due and owing by each of them to the United States of America for calendar year 2000, as set forth below, by various means, including among others:

- a) designing and then implementing a tax shelter transaction which they knew had no reasonable possibility of generating a profit;
- b) using that tax shelter to generate tax losses they knew could not properly be deducted on their respective tax returns;
- c) creating entities that served no legitimate business purpose, but were used merely to obtain tax benefits;
- d) preparing and executing false and fraudulent documents intended to deceive the IRS, including but not limited to transactional documents and a Certificate of Facts;
- e) preparing and causing to be prepared, signing and causing to be signed, and filing and causing to be filed a false and fraudulent U.S. Individual Income Tax Return, Form 1040, which substantially understated each defendant's taxable income and tax due and owing; and
- f) taking various steps to conceal from the IRS the true facts relating to the tax shelter, including providing false information in response to IDRs sent by the IRS.

Count	Defendant/ Taxpayer	Return	Approx. Amount of Fraudulent Underpayment	Approx. Filing Date
5	ROBERT COPLAN	2000 Form 1040	\$ 291,913	April 15, 2001
6	MARTIN NISSENBAUM	2000 Form 1040	\$ 340,262	April 16, 2001
7	RICHARD SHAPIRO	2000 Form 1040	\$ 201,565	August 16, 2001

(Title 26, United States Code, Section 7201)

COUNT EIGHT

(Obstruction of the IRS)

The Grand Jury further charges:

128. The allegations set forth in paragraphs 1 through 10, 13 through 20, 27 through 34, and 68 through 82, 96 and 97 are repeated and realleged as if fully set forth herein.

129. On or about September 25, 2003, in the Southern District of New York and elsewhere, MARTIN NISSENBAUM, the defendant, unlawfully, wilfully, and knowingly did corruptly obstruct and impede, and did endeavor to obstruct and impede, the due administration of the Internal Revenue Code; to wit, in response to IDR #2, NISSENBAUM caused the false and misleading statements set forth in paragraph 82, above, to be submitted to the IRS on behalf of himself and ten other E&Y partners.

(Title 26, United States Code, Section 7212).

COUNT NINE

(Obstruction of the IRS)

The Grand Jury further charges:

130. The allegations set forth in paragraphs 1 through 10, 13 through 20, 27 through 34, 64, 65, 96 and 97 are repeated and realleged as if fully set forth herein.

131. On or about July 17, 2001, in the Southern District of New York and elsewhere, ROBERT COPLAN, the defendant, unlawfully, wilfully, and knowingly did corruptly obstruct and impede, and endeavor to obstruct and impede, the due administration of the internal revenue laws, to wit, with knowledge that one of E&Y's COBRA transactions was

then under audit, and that the IRS had formally requested production of COBRA promotional materials, COPLAN sent an email directing PFC professionals and others throughout the country immediately to “delete and dispose of” COBRA materials in their files and their computers.

(Title 26, United States Code, Section 7212).

COUNT TEN

(False Statements To The IRS)

The Grand Jury further charges:

132. The allegations set forth in paragraphs 1 through 10, 13 through 18, 21 through 67, 96 and 97 are repeated and realleged as if fully set forth herein.

133. On or about June 12, 2002, in the Southern District of New York and elsewhere, BRIAN VAUGHN, the defendant, in a matter within the jurisdiction of the executive branch of the Government of the United States, unlawfully, wilfully, and knowingly made materially false, fictitious and fraudulent statements and representations, to wit, in connection with an examination by the IRS of tax shelters marketed by Ernst & Young, VAUGHN gave the false testimony underlined below:

(Page 22, line 17)

Q. How did you get involved in these digital option transactions?

A. Mainly from our clients. Our clients, as I mentioned before, were getting bombarded by a couple of other accounting firms. And they would – it would bubble up to us, and come to the client service professional, and they’d call and say, “Hey, look. My client is being called on on these various solutions. We need an answer. Does it work or doesn’t it? And what is the firm’s position?” And so that’s how we were first introduced to the concept. Other time – to my knowledge, there was one other time when a fund was created, and certain of our

(a)

high net worth individuals were offered the potential to go into the fund, so that came through a broker-dealer.

* * * *

(Page 31, line 13)

- Q. [D]o you know anything about the fees that investors paid to enter into these [digital option] contracts? I already asked about the premium amounts, but do you know any fees that were paid to [financial institution], fees that were paid to [bank]? Were there any standard fees?
- A. Like I said, I think the counterparty did take a fee for the execution. There was a tax fee for the tax advice, and for – for future examination, if they were to be examined. We would forecast what we thought our time and expense would be to go through an examination process with that specific client. So our – there was a tax fee paid to Ernst & Young, there was a fee paid to the attorney, whichever attorney they chose to issue the tax opinion. And then there was, I'm sure, the investment fees that – whoever the counterparty would charge.
- Q. Was Ernst & Young's fees fixed fees?
- (c) A. It was fixed per client, but they were negotiated fees. As always, we try to start with our 100 percent per diem billing rates, but we never somehow got there. So but on all our solutions, whether it is wealth management, which is our personal CFO service, whether its investment advisory services, we always do a front-end work plan, sort of a budget, on here is the various professionals in the national group, in the local group, in the area groups, what their billing rates are, how much time that we would think to expend on a particular transaction. And then we try to back that into a fixed fee, because we found our clients liked fixed fees rather than open-ending, you know, invoice, invoice me at your will, and it keeps coming. So all of our engagement letters, for whatever we do, is fixed.

* * * *

(Page 49, line 10)

- Q. Who developed the structure ... of the digital currency option trade?
- A. The digital option trade, I believe, was – [Law Firm] actually approached one of

our clients with that. . . . [I]t was either [Law Firm], or it was Arthur Andersen had approached one of our clients that had this particular program, then it came bubbling up to us. Then we had to assess whether our client should go into this particular transaction. . . .

Q. So did E&Y develop its own brand?

(d) A. No. The only thing we do is, again, we look at the tax issue surrounding how the proposed structure is. And if we can get to a filing position, then we will tell the client service professionals that we believe we can sign this return. But we don't –

(e) we – since day one, the only solutions that I know that we have created ourselves is wealth management solutions, investment advisory services, equity risk management services. But there was no tax strategy, per se, that was developed internally by our individual tax practice.

* * * *

(Page 53, line 4)

Q. Are you familiar with BCP Trading and Investments, LLC?

A. BCP Trading and Investments, LLC? That sounds like – sounds like one of the funds that Chuck Bolton used for one of the, seems like, one of the clients for the swap, but I can't recall specifically. Sounds like a Bolton entity.

Q. So you don't know anything about the structure of the LLC of BCP Trading and Investments, LLC?

(f) A. All I know was to the best of my knowledge, that entity was structured by Chuck Bolton as a private offering to clients, whether they were clients of Ernst & Young or clients of, you know, Chuck Bolton's, et cetera, to participate in foreign currency trading. That's my knowledge of it. . . . But I know that that was one where Chuck felt that he could take advantage of the dollar-yen movements and some Euro-yen movements, and felt that he came to us and said, look, I've got this private offering, a fund that I want to set up, and do you have any high net worth clients that could participate? I'm offering it to, you know, sort of a universe of people. That was my knowledge of it.

* * * *

(Page 61, line 11)

- Q. Were subject matter specialists involved in the digital currency option trade?
- (g) A. Oh, I'm sure. That's why I was trying to remember who the right subject matter person on that would have been. I – but yes. There had to have been a subject matter expert involved in every – if it was – involved a tax strategy that the client was looking at, then it had to go to the appropriate subject matter expert on that.

* * * *

(Page 67, line 3)

- Q. Did E&Y ever develop its own investment strategies that it would then pitch to its own clients, similar to the way you described it earlier, that, let's say, Arthur Andersen went to one of your clients?
- A. Well, we have investment advisory services, which we believe is our propriety [sic] investment advisory solution. That's where we've gone out and we've contacted what we believe is the best agreed money managers, we got them to reduce their minimums that a client could get into that specific manager, and we got them to reduce their fees that they would charge off the street, because we felt our clients – we could bring a lot of clients to them. . . . So that is our investment – when you say have we developed an investment alternative for our clients, that is one that we developed in-house and we are taking out to our clients to market for investment advisory services.
- Q. But the digital currency option trade did not come out of that group?
- A. No. No. That was, again, brought to us by an outside organization.
- Q. And who was that?
- (h) A. Again, Chuck Bolton came to our clients with a fund to participate in. That was one instance. And, again, the other instance is when a client was shown a digital option strategy, and [Bank] had been, you know, the counterparty with that.

* * * *

(Page 70, line 21)

- Q. So it would be someone like Bolton that would develop [a swap transaction] and bring it to E&Y?

- (i) A. Yeah. That would be for one instance, yeah. Bolton would have a – I mean, because they did. They created a fund, and they brought it to a client – the client of the firm. And of course, that client service professional says hey, what do you think of this. And that’s you know, how the process works.

* * * *

(Page 71, line 22)

- Q. Did Bolton bring . . . the digital currency option trade to E&Y? Was it Bolton who approached the client of yours?
- (j) A. Bolton approached the client with a fund, with a private offering memorandum that dealt with foreign currency trading, which included some, you know – with the digital, whether American, European, it was a foreign currency fund.

* * * *

(Page 84, line 4)

- Q. How did you – how did E&Y determine its fees when it came – or did it – with its consulting fees for, let’s say, is it done on a transaction-by-transaction basis?
- A. Client by client.
- Q. Client by client. For providing tax advice on –
- A. Yes.
- Q. – let’s say, that – the digital currency option trade, the client came to you and said, “Can you look at this and let me know what you think,” how would you determine the fees?
- (k) A. Time and expense, and forecasting, again, as I mentioned before. Part of our engagement was not only to consult with them to give them tax advice on their specific investment, but also to build in, if we thought there was a high likelihood of examination, we were not just going to, you know, bill them again. So we had to try to best estimate what our fee is going to be, based on the time that we would incur from a national perspective, you know, defending the client.
- Q. And –
- A. Then we would fix – then it would be a fixed fee.
- Q. How would you determine the fixed fee? Was there any kind of formula used?

(l) A. Well, again, with each – every time that we go about working on a solution, we come up with a budget, sort of a work plan. It involves the level of personnel assigned to it, their appropriate billing rate, the hours that we estimate it's going to expend with that particular client, and then we come to our best guess of what that is from a fixed fee standpoint, and the margin that we want, you know, from a business perspective. If we want a 15 percent margin or 10 percent margin, that affects, obviously, from a pricing standpoint, what we want. We got to have a business, you know.

Q. None of that fee was ever based on a tax savings?

(m) A. No. We never – our policy as a firm is not to take a percentage of tax savings. So we, from an individual perspective, – and I can't speak to what other groups in Ernst & Young but only the PFC practice, we take no contingent fees and we don't take a percentage of tax savings. Now, the fixed fee may be a percentage of their investment, because a lot of times the private offering memorandum will have to state all fees associated with it. And the normal rule of thumb on how private offering memorandums is always related back to the fixed fee as a percentage of your invested capital.

* * * *

(Page 87, line 8)

Q. Let's go back to the Bolton fund, that type of transaction that then went to your client, and you did your review, came back with a more likely than not, and then determined that it could work for X amount of clients, how would you then bill your time when you presented it to your – the various clients?

(n) A. Client by client. . . . So it's all determined in about – the team assigned to that client, how many hours they anticipate there's an amortization of the research and development time, there's forecast for defense. But really, it's client by client by client, because we don't know how this particular investment is going to fit with their overall financial plan. . . . I have never seen a cookie-cutter deal. You know, I've never seen, you know, let's just replicate this, because every client's demands are so unique.

* * * *

(Page 100, line 11)

- Q. Do you know Robert Copeland [sic]?
- A. Yes. He is our subject matter expert in estate and gift tax area.
- Q. So would he have been involved in this transaction [CDS Add-On]?
- (o) A. If it dealt – maybe tangentially, because his expertise is estate and gift. I think – I’m sure – I’m sure Bob was involved to some extent. To what his personal involvement was, I don’t know. Because anything dealing, you know, with a fund that affects a person’s gift and estate tax ramifications, definitely Bob could have been called. . . . Bob probably did get called, but I don’t know. I don’t know.

* * * *

(Page 103, line 14)

- Q. Did E&Y ever come out with a more likely than not conclusion to any deal that he –
- A. One.
- Q. One. Okay. Which one?
- A. That was a swap with Bolton.
- Q. What was Bolton’s role in the swap?
- A. Execute. They executed the swap. . . .
- Q. Do you know what type of entity would have been used to facilitate the swap?
- A. I think most of the time it was either LLCs or limited partnerships or general partnerships.
- Q. Do you know why you would use that type of entity?
- (p) A. Client choice. Either client choice or the recommendation of client counsel.

* * * *

(Page 107, line 20)

- Q. And there was the name of someone that you had mentioned before that had left E&Y that worked – Belle Six, I think you –
- A. Yeah. She was an employee I think in 1998, and then pursued other –
- Q. Where did she go?
- (q) A. I couldn’t tell you. I don’t know where she is.

* * * *

(Page 126, line 12)

- Q. So who would bring all the parties to the transaction together, be it, you know, the broker-dealer, who would bring that entity in?
- (r) A. Well, for instance, on the fund that we talked about earlier, [Company X] already had all the pieces together from the investment standpoint. And so they were bringing the transaction to us. So they had already put – you know, they had put everything together from the investment standpoint, the private offering memorandum, et cetera.

* * * *

(Page 136, line 6)

- Q. Do you recall what the probability of a tax benefit was?
- (s) A. No, I don't recall.

* * * *

Page 138, line 21)

- Q. Would you give any advice to clients as to timing of exiting?
- (t) A. I think that was – well, only from an investment standpoint. Obviously, if they were making money, stay in. If they were losing money, let's look at alternatives.
- Q. In terms of tax benefits, though?
- (u) A. No. I mean, this was an investment for the client. So our advice was centered around if you're going to – if you believe this is a good investment and it makes sense, stay in. Continue to do, you know, to do the digital trading, do the foreign currency trading. If it doesn't make sense, let's think about exiting and how should we exit.

* * * *

(Page 139, line 22)

- Q. Do you know if clients withdrew from it?
- A. Yes. I do know clients withdrew from it.

- Q. Do you know what the basis would have been for withdrawing from it?
- (v) A. Lack of profit.

* * * *

(Page 142, line 9)

- Q. When you were determining the entrance, . . . [h]ow would you calculate what their contribution would be?
- A. I think a lot was dictated on how much percentage profits that they wanted in the fund, and how much they felt comfortable with contributing.
- Q. What are the types of assets that they were contributing?
- A. If I remember the fund, the fund was a digital, foreign currency digital program. . . .
- Q. Where did they get the options from?
- (w) A. Well, the digital options were purchased as part of their, from the investment standpoint, as part of their alternative investment, you know, that was just part of their investing.

* * * *

(Page 165, line 6)

- Q. Are you aware of any of the listed transactions that your clients engaged in prior to them being listed?
- A. [Looking at Notice 2001-51] Yes.
- Q. Do you know which ones?
- A. CDS, I think, just got listed, if I remember right, is a listed transaction, the swap transaction. . . .
- Q. Are you familiar with any of the other ones? . . . What about No. 11, the Notice 2000-44?
- (x) A. Inflating the basis of partnership interests? I don't think we did any inflation of partnership interest.

* * * *

(Page 169, line 8)

Q. I'm going to get off the list of transactions and ask whether at any time did you ever consult an E&Y database for strategy?

A. An E&Y database for strategy. Trying to think. Database. We have – if the client asked for a – trying to think what an example would be – an engagement letter, then we would have – there is a repository for engagement letters so that we wouldn't have to duplicate that effort. . . .

Q. Where would that be?

A. That is in a just – I think it's a general PFC database. And you're talking to someone that's administratively, again, very weak in this. . . . So, yeah, I do think there's a PFC database that would have engagement letters there.

Q. Would there be a database where after you review, say, the currency, the fund, where you could let everyone out there in the country know that hey, this is a good vehicle for your clients if you have someone that wants it?

(y) A. Other than email? I don't know. I mean, if a client – see, everything was driven from the client's perspective. So if the client came to the client service professional and said, you know, we've got this that's – you know, got this fact pattern, or whatever, and then they call the subject matter expert, the subject matter expert said send them an email, look, this has been done for another client and, you know, the fact pattern sounds similar, you may want to investigate this particular deal[.]

* * * *

(Page 176, line 4)

Q. [T]ake just a digital currency option trade as an example, would that fit into the definition of a solution?

(z) A. That would be a one off tax strategy. So, in other words, there would be no database or this thing formed for digital option, because it was a one off investment fund that was produced by a third party that came to us. Most of our solutions, I think almost all the solutions are internally developed. So a solution is just a way that Ernst & Young has been doing a service, it needs to be standardized. If it was a tax strategy that was brought to us by a third-party vendor, that's not a solution per se. We used to call it just, you know, a tax strategy.

- Q. Did Ernst & Young create its own tax strategies?
- (aa) A. Unfortunately, no. We – the only, I guess, strategies, per se, a Chuck Bolton would have brought to us.

* * * *

Page 186, line 22)

- Q. Would – back to the fund, the Bolton fund . . . – the eight to ten that you actually were involved in . . . did each client approach E&Y to engage in the fund?
- (bb) A. For financial planning assistance. They would have come to their relationship person and said, you know, for whatever reason I've got this fact pattern. And then the relationship person would say, "Hey, Brian, you know, this is the fact pattern." Well, if I was aware this fund was being offered, I'd say, "Well, look, you need to probably check with Chuck Bolton, see if the facts of this make sense for you." If it was an investment planning professional that had done an asset allocation, said we need to look at a hedge fund, you know, Chuck Bolton's hedge fund at that time would have been one that they probably would have considered. So it really just, you know, it really depended upon the risk tolerance of the client from an investment perspective and whether a hedge fund fit in their asset allocation.

(Title 18, United States Code, Section 1001).

COUNT ELEVEN

(False Statements To The IRS)

The Grand Jury further charges:

134. The allegations set forth in paragraphs 1 through 10, 13 through 18, 21 through 67, 96 and 97 are repeated and realleged as if fully set forth herein.

135. On or about June 20, 2002, in the Southern District of New York and elsewhere, ROBERT COPLAN, the defendant, in a matter within the jurisdiction of the executive

branch of the Government of the United States, unlawfully, wilfully, and knowingly made materially false, fictitious and fraudulent statements and representations, to wit, in connection with an examination by the IRS of tax shelters marketed by Ernst & Young, COPLAN gave the false testimony underlined below:

(Page 24, line 10)

Q. Who produced the materials [to be distributed to clients] for the Bolton transaction. . . . a description of the transaction that you would give to investors before they invest --

A. Yeah. On the Bolton transaction, there were no materials given. That was just explained. . . . I believe 1 office did produce something, and it was on their own and without national involvement. . . .

Q. What office was it?

A. Seattle.

Q. Did you review any of those materials?

A. I did after I became aware of them, but not for distribution. In other words, I basically said, these are not to be distributed.

Q. And why did you say they were not to be distributed?

(a) A. We didn't see the need to, and anything – or even show it to clients. We didn't think the transaction was that complicated, to be honest with you, so we only really had it for internal purposes.

* * * *

(Page 34, line 9)

Q. And who was the counterparty in most of these [CDS Add-On transactions]?

A. I believe it was [Financial Institution] in both transactions.

Q. And [Financial Institution] is a U.S. entity?

A. Again, I've become aware there was some confusion about that On the [Company X] transaction, it was really being – all the investments aspects of it were being done in connection with the existing partnerships. And those existing partnerships had trading accounts that were doing exotic option trading and other trading, and so – and Ernst & Young had nothing really to do with the operation of that partnership.

(b)

Q. M-hm.

A. So Bolton was the asset manager. Bolton was not necessarily at the time, but they became the general partner also of those accounts during the period in question. And so they were leading the investment decisions of who to use, and they were using a trader who specialized in these type of currency options. And so we

(c) really didn't – we, Ernst & Young, really didn't have involvement in the decisions that the general partner made as to who to use to do the trading, how to structure those trades. It was really their investment decision and their decision as general partner. They didn't have to ask us anything.

* * * *

(Page 38, line 11)

Q. What were the risks on the tax transaction?

A. That the IRS would disagree, that you had basis in the partnership.

Q. What did you think the IRS would – just on the basis issue alone, that's what you thought the issue would be?

A. Yeah. But I think in the explanations that have been put forth of the facts and amnesty disclosures, et cetera, on this transaction, the surrounding facts were such that when we analyzed it, we looked at the fact that the partnerships were existing partnerships, they had been doing some of this trading, and that there was going to be a transfer of a portion of the trading accounts to this [Financial Advisor] outfit for management, and he said, I'm not going to manage a whole bunch of these little accounts, I'm going to put all of these things into an LLC so I can do 1 account trading for these options. And it was 1 of those circumstances where his tax planner – as we say, we're aware of this idea that's out there. We hear about the concept of transferring a long and a short option that aren't matched and getting basis and not having to reduce it for the liability, and so here was kind of a fortuitous circumstance where if these accounts are going to be transferred into an entity anyway, that it's a matter of taking the tax position, because along with that transfer, if someone felt appropriate to do it.

* * * *

(Page 62, line 7)

Q. So how did Bolton get involved in the option transaction?

A. Bolton got involved – this was later on after David Smith brought the idea to us. So in other words, we had the idea. That's why I said at some point, we kind of married an idea with facts in the Bolton transaction, so that it was what we did with Bolton. But we had the idea at some previous time from David Smith.

Q. Okay. So maybe I asked this: How did Bolton actually come to do the transaction? Did you have – is this based on a preexisting relationship with Bolton?

A. Yeah. I mean, I said we – Bolton was involved in the swap partnerships.

Q. Okay.

A. And so they were involved as the asset allocators and the investment folks. And they were dealing with these trading-type people like [Financial Advisor] is the 1 involved.

(e) And so we're the tax advisors, and we said, hey, if you are happening to be forming these – transferring these trading accounts over to [Financial Advisor] and he's going to put them in an LLC, we know this tax idea. That's kind of what I said before.

* * * *

(Page 98, line 6)

Q. Were clients concerned about the large capital gain at the end of the [CDS] transaction in that they would have a large amount to pick up in income that year?

(f) A. That was – well, they weren't sure that that would happen, because they had to make a decision on the economic side to – they would have to decide to early-terminate the swap, because the swap was scheduled to run for 18 months. And so a decision was required on their part or the counterparties' part to terminate the swap prior to the majority. Otherwise, you'd have ordinary income on the back end.

Q. Did – do you know, did all the partnerships terminate early?

A. I believe they did.

* * * *

(Page 118, line 116)

Q. Was there a reason why [the Add-On transaction] was done through an LLC and not for the Jenkins partnerships for lack of a better description?

A. Well, as I think I explained, the – well, the Jenkins came first. They were done with individual folks forming a partnership. And they did their ... currency contracts and contributed them to partnerships. The [Add-On] transaction wasn't really done that way. It was done based on the fact that the partnerships were transferring their trade – I mean, it really was a fact that existed prior to the tax idea. In other words, the LLC was formed as an LLC because of Mr. [K's] interest in forming an LLC for all those trading accounts. . . . For the – for all those partnerships that were doing this type of trading that Bolton said, we can't use [Financial Institution] anymore to do this kind of trading, we've got to move the trading account over to [Financial Advisor]. And so they moved it and he said, if I'm going to do this trading for you, I'm going to have all these accounts in 1 entity.

* * * *

(Page 139, line 12)

Q. Who would pay E and Y fees [for PICO], the individual or the S Corp?

A. We had an engagement letter with the individual.

Q. The individual was responsible for paying the fees?

(h) A. We were paid by the individual. We also received a fee from [Company Z] for consulting with them on the transaction. . . . We were advising them on the tax aspects of the results of investors investing in these types of S corporations.

(Title 18, United States Code, Section 1001).

COUNT TWELVE

(Tax Evasion of David L. Smith)

The Grand Jury further charges:

136. The allegations set forth in paragraphs 11, and 21 through 23 are repeated and realleged as if fully set forth herein.

137. During 1997 and 1998, before defendant DAVID L. SMITH founded PCMG, he was the part owner of a so-called “investment advisory” firm referred to herein as “Q Advisors.” At that time, Q. Advisors was involved in designing, marketing and implementing tax shelters, including CDS.

138. As of January 1998, SMITH owned his interest in Q. Advisors through two layers of entities. The first entity was S&L Advisors, LLC (S&L Advisors), which was a 50% owner of Q. Advisors. S&L Advisors, in turn, was owned by two other entities: 1) the Smith Family Trust (the 99% owner of S&L Advisors), a pass-through entity for tax purposes, which was controlled by SMITH; and 2) S&L Advisors, Inc. (the 1% owner of S&L Advisors), another pass-through entity which was also controlled by SMITH.

139. In 1998, S&L Advisor’s share of the income earned by Q. Advisors was \$18.4 million. Based on the structure described in paragraph 138, above, the \$18.4 million paid to S&L Advisors should have passed through to defendant DAVID L. SMITH, and been reported as income by SMITH on his individual income tax return.

140. During the period from mid-1998 through at least July 2003, defendant DAVID L. SMITH took numerous steps to evade the tax on the \$18.4 million paid by Q. Advisors to S&L Advisors. Among other things:

a) In mid-June 1998, SMITH set up a Cayman Islands entity called “Aegis Capital Investments Ltd. (“Aegis”), which was controlled by SMITH, but was designed to appear as though SMITH had no control over it or relationship to it;

b) In mid-June 1998, SMITH set up one or more accounts in the name of Aegis in the Cayman Islands;

c) On or about June 26, 1998, SMITH engaged in a sham sale of the Smith Family Trust’s 99% interest in S&L Advisors to Aegis, a step which appeared to give an unrelated company the right to receive SMITH’s portion of the income from Q. Advisors. SMITH thereafter directed Q. Advisors to transfer S&L Advisors’ income to a Cayman Island account opened in the name of Aegis;

d) In August 1998, SMITH arranged to implement a CDS-type transaction on behalf of S&L Advisors, using a \$20 million swap (including an \$18 million “loan” from a bank) to defer from 1998 to 1999 the tax liability on the income from Q. Advisors;

e) On or about January 5, 1999, the day S&L’s swap terminated, SMITH directed that the cash proceeds of the termination payment be transferred to the Aegis account in the Cayman Islands;

f) On or about October 15, 1999, SMITH signed and filed a 1998 tax return (a Form 1065) on behalf of S&L Advisors, on which he reported the \$18.4 million in income from Q. Advisors, but also reported \$19.9 million in deductions from the CDS swap, resulting in zero taxable income;

g) Although SMITH knew that the proceeds of S&L’s CDS swap had been paid to S&L Advisors in January 1999, and that the full amount of the termination payment

was reportable as income to S&L Advisors in 1999, SMITH indicated on the 1998 return he signed and filed on behalf of S&L Advisors that the return was a “Final return,” thus indicating to the IRS that S&L anticipated no reportable income in 1999;

h) On or about October 15, 1999, SMITH signed and filed a 1998 individual income tax return (Form 1040) on behalf of himself and his spouse, on which he reported zero taxable income and claimed a refund;

i) Although SMITH owned and controlled one or more Aegis accounts in the Cayman Islands during 1998, on his 1998 individual income tax return, where the return asked whether at any time during 1998 SMITH had “an interest in . . . or other authority over a financial account in a foreign country,” SMITH indicated “No.”

j) In or about April 2002, an individual income tax return for 1999 was prepared for SMITH by a tax preparer in New York, New York. SMITH filed but did not sign the return. The return did not report the \$19.9 million swap termination payment made to S&L Advisors on January 5, 1999.

k) On the 1999 individual tax return filed by SMITH in April 2002, where the return asked whether at any time during 1999 SMITH had “an interest in . . . or other authority over a financial account in a foreign country,” SMITH indicated “No.”

l) On or about November 5, 2002 and November 6, 2002, in connection with a civil audit of SMITH’s tax liabilities, SMITH was interviewed by an IRS revenue agent. During that interview, SMITH told the revenue agent that he had sold his interest in S&L Advisors to Aegis, and that SMITH had no interest in Aegis.

m) On or about December 1, 2002, SMITH signed and filed his individual income tax return for 2000. Where the return asked whether at any time during 2000 SMITH had “an interest in . . . or other authority over a financial account in a foreign country,” SMITH indicated “No.”

n) On or about July 19, 2003, SMITH signed a declaration, under penalties of perjury, that he had examined his 1999 individual income tax return and that, to the best of his knowledge, it was true, correct and complete.

Statutory Allegations

141. From in or about January 1, 1998, through at least on or about July 19, 2003, in the Southern District of New York and elsewhere, DAVID L. SMITH, the defendant, unlawfully, wilfully and knowingly did attempt to evade and defeat a substantial part of the income tax due and owing by him to the United States of America, on \$18.4 million he earned from Q. Advisors, by various means, including among others:

- a) creating and utilizing an off-shore entity designed to disguise his receipt and control of the \$18.4 million from Q. Advisors;
- b) entering into a tax shelter transaction to defer his tax liability on the \$18.4 million from 1998 to 1999, with the intent not to report the income in 1999;
- c) causing to be prepared, and causing to be signed and filed, false and fraudulent U.S. Individual Income Tax Returns, Forms 1040, which understated his taxable income and the tax due and owing thereon, and which concealed his interest in, and authority over, the foreign bank account or accounts into which the income from Q. Advisors had been

transferred; and

d) making false statements to an IRS revenue agent in connection with an audit of his tax liability.

(Title 26, United States Code, Section 7201).

COUNT THIRTEEN

(False 1999 Tax Return Filed by David L. Smith)


142. The allegations set forth in paragraphs 11, 21 through 23, and 136 through 140 are repeated and realleged as if fully set forth herein.

143. From in or about April 2002, up to and including July 19, 2003, in the Southern District of New York and elsewhere, DAVID L. SMITH, the defendant, unlawfully, willfully and knowingly did make and subscribe a U.S. Individual Income Tax Return, Form 1040, on behalf of himself for calendar year 1999, which was verified by a written declaration that the return was made under penalties of perjury, which was filed with the Internal Revenue Service, and which SMITH did not believe to be true and correct as to every material matter, in that, among other things, the return indicated that during 1999, SMITH had no interest in, or other authority over, a financial account in a foreign country.

(Title 26, United States Code, Section 7206(1).)



FOREPERSON



MICHAEL J. GARCIA
United States Attorney